GSI GROUP INC
Form 10-Q
August 11, 2011
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

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

For the quarterly period ended July 1, 2011

Or

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

For the transition period from to

Commission File No. 001-35083

GSI Group Inc.

(Exact name of registrant as specified in its charter)

New Brunswick, Canada **(State or other jurisdiction of** **incorporation or organization)**	**98-0110412** **(I.R.S. Employer** **Identification No.)**
125 Middlesex Turnpike **Bedford, Massachusetts, USA** **(Address of principal executive offices)**	**01730** **(Zip Code)**

(781) 266-5700

(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 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 x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

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

Large accelerated filer	¨	Accelerated filer	¨
Non-accelerated filer	¨ (Do not check if a smaller reporting company)	Smaller reporting company	x

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

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Section 12 , 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes x No ¨

As of July 29, 2011, there were 33,359,764 of the Registrant s common shares, no par value, issued and outstanding.

Table of Contents

GSI GROUP INC.

TABLE OF CONTENTS

Item No.		Page No.
PART I FINANCIAL INFORMATION		
ITEM 1.	FINANCIAL STATEMENTS	3
	CONSOLIDATED BALANCE SHEETS (unaudited)	3
	CONSOLIDATED STATEMENTS OF OPERATIONS (unaudited)	4
	CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)	5
	NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (unaudited)	6
ITEM 2.	MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS	27
ITEM 3.	QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK	40
ITEM 4.	CONTROLS AND PROCEDURES	40
PART II OTHER INFORMATION		
ITEM 1.	LEGAL PROCEEDINGS	41
ITEM 1A.	RISK FACTORS	42
ITEM 2.	UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS	42
ITEM 3.	DEFAULTS UPON SENIOR SECURITIES	42
ITEM 4.	[REMOVED AND RESERVED]	42
ITEM 5.	OTHER INFORMATION	42
ITEM 6.	EXHIBITS	42
SIGNATURES		44

Table of Contents

PART I FINANCIAL INFORMATION

Item 1. Financial Statements

GSI GROUP INC.

CONSOLIDATED BALANCE SHEETS

(In thousands of U.S. dollars, except share data)

(Unaudited)

	July 1, 2011	December 31, 2010
ASSETS		
Current Assets		
Cash and cash equivalents	$ 73,999	$ 56,781
Accounts receivable, net of allowance of $563 and $696, respectively	58,339	55,110
Income taxes receivable	21,984	21,920
Inventories	71,112	66,721
Deferred tax assets	4,319	4,226
Deferred cost of goods sold	3,138	7,789
Prepaid expenses and other current assets	6,125	5,580
Total current assets	239,016	218,127
Property, plant and equipment, net of accumulated depreciation of $59,379 and $55,336, respectively	43,623	45,402
Deferred tax assets	1,729	1,445
Other assets	5,799	4,476
Intangible assets, net	49,269	53,139
Goodwill	44,578	44,578
Total Assets	$ 384,014	$ 367,167
LIABILITIES AND STOCKHOLDERS EQUITY		
Current Liabilities		
Accounts payable	$ 19,465	$ 19,766
Income taxes payable	2,835	1,785
Accrued compensation and benefits	10,939	7,988
Deferred revenue	7,195	15,006
Deferred tax liabilities	11	
Other accrued expenses	14,782	14,717
Total current liabilities	55,227	59,262
Debt	108,107	107,575
Deferred revenue	360	402
Deferred tax liabilities	8,486	8,373
Accrued restructuring, net of current portion	471	769
Income taxes payable	7,275	6,644
Accrued pension liability	2,663	3,044
Other liabilities	1,490	2,420
Commitments and contingencies (Note 12)		
Stockholders Equity:		

Common shares, no par value; Authorized shares: unlimited; Issued and outstanding: 33,352,192 and 33,342,169 respectively	423,856	423,856
Additional paid-in capital	16,415	14,655
Accumulated deficit	(240,460)	(256,733)
Accumulated other comprehensive loss	(269)	(3,429)
Total GSI Group Inc. stockholders equity	199,542	178,349
Noncontrolling interest	393	329
Total stockholders equity	199,935	178,678
Total Liabilities and Stockholders Equity	$ 384,014	$ 367,167

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

GSI GROUP INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands of U.S. dollars or shares, except per share amounts)

(Unaudited)

	Three Months Ended		Six Months Ended	
	July 1, 2011	July 2, 2010	July 1, 2011	July 2, 2010
Sales	$ 101,370	$ 85,737	$ 193,228	$ 200,352
Cost of goods sold	56,377	47,681	108,341	113,258
Gross profit	44,993	38,056	84,887	87,094
Operating expenses:				
Research and development and engineering	7,946	7,399	16,117	14,764
Selling, general and administrative	21,254	17,573	40,522	35,145
Amortization of purchased intangible assets	987	1,126	1,979	2,254
Restructuring, restatement related costs and other	(61)	1,011	122	1,679
Post-emergence professional fees	94		233	
Total operating expenses	30,220	27,109	58,973	53,842
Income from operations	14,773	10,947	25,914	33,252
Interest income	19	25	39	50
Interest expense	(3,414)	(5,747)	(7,084)	(11,555)
Foreign exchange transaction gains (losses), net	(123)	(106)	(815)	263
Other income (expense), net	358	1,081	1,388	1,686
Income from operations before reorganization items and income taxes	11,613	6,200	19,442	23,696
Reorganization items		(10,617)		(20,247)
Income (loss) from operations before income taxes	11,613	(4,417)	19,442	3,449
Income tax provision	1,538	638	3,105	2,463
Consolidated net income (loss)	10,075	(5,055)	16,337	986
Less: Net income attributable to noncontrolling interest	(9)	(11)	(64)	(52)
Net income (loss) attributable to GSI Group Inc.	$ 10,066	$ (5,066)	$ 16,273	$ 934
Net income (loss) attributable to GSI Group Inc. per common share:				
Basic	$ 0.30	$ (0.32)	$ 0.49	$ 0.06
Diluted	$ 0.30	$ (0.32)	$ 0.48	$ 0.06
Weighted average common shares outstanding basic	33,478	15,967	33,464	15,960
Weighted average common shares outstanding diluted	33,595	15,967	33,564	15,981

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

Table of Contents

GSI GROUP INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands of U.S. dollars)

(Unaudited)

	Six Months Ended	
	July 1, 2011	**July 2, 2010**
Cash flows from operating activities:		
Consolidated net income	$ 16,337	$ 986
Adjustments to reconcile net income to net cash from operating activities:		
Depreciation and amortization	7,699	7,505
Provision (recoveries) for uncollectible receivables	(61)	(591)
Provision for inventory obsolescence	3,259	3,414
Share-based compensation	1,760	1,090
Deferred income taxes	(253)	149
Earnings from equity investment	(1,413)	(622)
Loss on disposal of assets	85	40
Gain on sale of auction rate securities		(988)
Non-cash interest expense	459	
Non-cash restructuring charges	34	40
Changes in operating assets and liabilities:		
Accounts receivable	(2,620)	(5,044)
Inventories	(6,455)	(2,074)
Deferred cost of goods sold	4,651	23,753
Prepaid expenses and other current assets	(451)	471
Deferred revenue	(7,853)	(39,387)
Accounts payable, accrued expenses and income taxes receivable and payable	3,834	26,136
Other non-current assets and liabilities	(1,122)	(333)
Cash provided by operating activities	17,890	14,545
Cash flows from investing activities:		
Purchases of property, plant and equipment	(1,698)	(1,196)
Proceeds from the sale of auction rate securities		11,408
Cash provided by (used in) investing activities	(1,698)	10,212
Cash flows from financing activities:		
Payments for debt issuance costs		(513)
Cash used in financing activities		(513)
Effect of exchange rates on cash and cash equivalents	1,026	(199)
Increase in cash and cash equivalents	17,218	24,045
Cash and cash equivalents, beginning of period	56,781	63,328
Cash and cash equivalents, end of period	$ 73,999	$ 87,373
Supplemental disclosure of cash flow information:		
Cash paid for interest	$ 6,605	$
Cash paid for income taxes	$ 1,106	$ 857
Income tax refunds received	$ 14	$ 1,753

Cash paid for reorganization items	$	$ 13,486
Supplemental disclosure of non cash financing activity:		
Debt issuance costs	$	$ 460
Issuance of PIK notes	$ 532	$

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

5

Table of Contents

GSI GROUP INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

AS OF JULY 1, 2011

(Unaudited)

1. Organization and Presentation

GSI Group Inc. (GSIG) and its subsidiaries (collectively the Company) design, develop, manufacture and sell laser-based solutions (consisting of lasers and laser systems), precision motion control devices and associated precision technologies, and semiconductor systems. The Company s technology is incorporated into customer products or manufacturing processes for a wide range of applications in a variety of markets, including: industrial, electronics, medical, semiconductor, scientific, and aerospace. The Company s products enable customers to make advances in materials and processing technology and to meet extremely precise manufacturing specifications. The Company exists under the laws of New Brunswick, Canada and serves principal markets in North America, Europe and Asia-Pacific. The Company realigned the structure of its internal organization during the three months ended April 1, 2011 in a manner that caused the composition of its reportable segments to change to the following three segments: Laser Products, Precision Motion and Technologies and Semiconductor Systems. The Company s reportable segment financial information has been restated to reflect the updated reportable segment structure for all periods presented. See Note 13 to Consolidated Financial Statements for further information about the Company s reportable segments.

Listing of Common Shares

On February 9, 2011, the Company s common shares were approved for listing on The NASDAQ Global Select Market. The Company s common shares began trading on The NASDAQ Global Select Market on February 14, 2011 under the symbol GSIG . As a result of the NASDAQ listing, the Company is no longer subject to the additional 2% per annum interest penalty relating to the reporting default under its 12.25% Senior Secured PIK Election Notes.

Basis of Presentation

These consolidated financial statements have been prepared by the Company in U.S. dollars and in accordance with U.S. generally accepted accounting principles, applied on a consistent basis.

The accompanying unaudited interim consolidated financial statements have been prepared pursuant to the rules and regulations of the United States Securities and Exchange Commission (SEC), and the instructions to Form 10-Q and the provisions of Regulation S-X pertaining to interim financial statements. Accordingly, certain information and footnote disclosures normally included in the financial statements prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) have been condensed or omitted pursuant to such rules and regulations. The consolidated financial statements and notes included in this report should be read in conjunction with the financial statements and notes included in the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2010, filed with the SEC.

The interim consolidated financial statements include the accounts of the Company. Intercompany transactions and balances have been eliminated. In the opinion of management, all adjustments and accruals necessary for a fair presentation have been made and include only normal recurring adjustments and accruals. The results for interim periods are not necessarily indicative of results to be expected for the year or for any future periods.

On December 29, 2010, the Company effected a one-for-three reverse stock split. All share data and per share amounts have been retroactively adjusted for the reverse stock split in the accompanying consolidated financial statements and notes thereto for all periods presented.

Basis of Consolidation

The consolidated financial statements include the accounts of GSI Group Inc. and its wholly owned subsidiaries. The accounts include a 50% owned joint venture, Excel Laser Technology Private Limited (Excel SouthAsia JV), since it is a variable interest entity and the Company is the primary beneficiary of the joint venture. The accompanying consolidated financial statements of the Company include the assets, liabilities, revenue, and expenses of Excel SouthAsia JV over which the Company exercises control. The Company records noncontrolling interest in its

consolidated statements of operations for the ownership interest of the minority owners of Excel SouthAsia JV. Financial information related to the joint venture is not considered material to the consolidated financial statements. Intercompany accounts and transactions have been eliminated.

Table of Contents

2. Bankruptcy Disclosures

On November 20, 2009, GSIG and two of its wholly-owned United States subsidiaries, GSI Group Corporation (GSI US) and MES International, Inc. (MES and, collectively with GSIG and GSI US, the Debtors), filed voluntary petitions for relief under Chapter 11 of the United States Bankruptcy Code in the United States Bankruptcy Court for the District of Delaware (the Bankruptcy Court) (the Chapter 11 Cases). On May 24, 2010, the Debtors filed with the Bankruptcy Court a modified joint Chapter 11 plan of reorganization for the Debtors, which was further supplemented on May 27, 2010 (as supplemented, the Final Chapter 11 Plan). On May 27, 2010, the Bankruptcy Court entered an order confirming and approving the Final Chapter 11 Plan and the Final Chapter 11 Plan became effective and the transactions contemplated under the Final Chapter 11 Plan were consummated on July 23, 2010.

Upon the Company s emergence from bankruptcy on July 23, 2010, the Company was not required to apply fresh-start accounting under Accounting Standards Codification (ASC) 852, Reorganizations (ASC 852). From the Company s bankruptcy filing on November 20, 2009 through the date of emergence, the Company prepared the consolidated financial statements in accordance with ASC 852 and on a going-concern basis, which assumed continuity of operations, realization of assets and satisfaction of liabilities in the ordinary course of business.

ASC 852 requires that the financial statements for periods subsequent to a Chapter 11 filing separate transactions and events that are directly associated with the reorganization from the ongoing operations of the business. Accordingly, all transactions (including, but not limited to, all professional fees, realized gains and losses and provisions for losses) directly associated with the reorganization and restructuring of the businesses are reported separately in the financial statements. All such costs are reported in reorganization items in the accompanying consolidated statements of operations for the three and six months ended July 2, 2010, with no comparable amounts for the three and six months ended July 1, 2011.

The Final Chapter 11 Plan deleveraged the Company s balance sheet by reducing debt and increasing stockholders equity. The financial restructuring was accomplished through a debt-for-equity exchange and by using the proceeds from a shareholder rights offering and cash on hand to reduce outstanding indebtedness. A summary of the significant transactions affecting the Company s capital structure as a result of the effectiveness of the Final Chapter 11 Plan is described in Note 2 to the Consolidated Financial Statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2010, filed with the SEC on March 30, 2011. Presented below is information concerning post-emergence professional fees and reorganization items, as applicable, incurred during the three and six months ended July 1, 2011 and July 2, 2010.

Post-Emergence Professional Fees

Post-emergence professional fees represent costs incurred subsequent to bankruptcy emergence for financial and legal advisors to assist with matters in finalizing the bankruptcy process, including bankruptcy claim matters. Post-emergence professional fees totaled $0.1 million and $0.2 million during the three and six months ended July 1, 2011, respectively, with no comparable amount during the three and six months ended July 2, 2010.

Reorganization Items

Reorganization items represent amounts that were recorded in the consolidated financial statements as a result of the bankruptcy proceedings. Reorganization items were incurred starting with the date of the bankruptcy filing. Reorganization items totaled $10.6 million and $20.2 million during the three and six months ended July 2, 2010, respectively, with no comparable amounts during the three and six months ended July 1, 2011.

3. Summary of Significant Accounting Policies

The accounting policies underlying the accompanying unaudited consolidated financial statements are those set forth in Note 3 to the Consolidated Financial Statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2010, filed with the SEC on March 30, 2011. Those policies are not presented herein, except to the extent that new policies have been adopted, or there is current period activity to disclose.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles 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 dates of the financial

statements and the reported amounts of sales and expenses during the reporting periods. On an ongoing basis, the Company evaluates its estimates, assumptions and judgments, including those related to revenue recognition; allowance for doubtful accounts; inventory costing and reserves; the assessment of warranty

Table of Contents

reserves; the valuation of goodwill, intangible assets and other long-lived assets; accounting for business combinations; share-based payments; employee benefit plans; accounting for restructuring activities; accounting for income taxes and related valuation allowances; and, accounting for loss contingencies. Actual results could differ significantly from those estimates.

Long-Term Investments

As of July 1, 2011 and December 31, 2010, the Company had liquidated all of its previously held auction rate securities. These auction rate notes were student loans backed by the federal government and were privately insured. During the three months ended July 2, 2010, the Company sold $10.0 million in par value of its auction rate securities valued at $8.0 million for $8.7 million in proceeds, which resulted in the recognition of realized gains of $0.7 million related to the sale of these securities. During the six months ended July 2, 2010, the Company sold $13.0 million in par value of its auction rate securities valued at $10.4 million for $11.4 million in proceeds, which resulted in the recognition of realized gains of $1.0 million related to the sale of these securities. The gains realized upon the sale of the auction rate securities are recorded in other income (expense), net in the accompanying consolidated statements of operations for the three and six months ended July 2, 2010. The Company determines the cost of a security sold and the amount to be reclassified out of accumulated other comprehensive income (loss) into earnings based on the specific identification method. During the three and six months ended July 2, 2010, the Company reclassified $0.4 million and $0.6 million, respectively, out of accumulated other comprehensive income (loss) into earnings related to the sale of the Company s auction rate securities. There were no auction rate securities held as of July 1, 2011 or December 31, 2010.

As of July 1, 2011 and December 31, 2010, the Company had a 25.1% equity investment in a privately held company located in the United Kingdom, valued at $3.7 million and $2.2 million at July 1, 2011 and December 31, 2010, respectively, and included in other assets in the accompanying consolidated balance sheets. The Company accounts for this investment using the equity method and recognized income of $0.4 million and $0.4 million for the three months ended July 1, 2011 and July 2, 2010, respectively, and $1.4 million and $0.6 million for the six months ended July 1, 2011 and July 2, 2010, respectively, which are included in other income (expense), net in the accompanying consolidated statements of operations.

Goodwill and Intangible Assets

As described in more detail in Note 3 to the Consolidated Financial Statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2010, filed with the SEC on March 30, 2011, the Company assesses goodwill and intangible assets for impairment on an annual basis and whenever events or changes in circumstances indicate impairment may exist. The Company completed annual tests for impairment as of the beginning of the second quarter of 2011 and 2010, and determined that goodwill and intangible assets were not impaired.

Revenue Recognition

The Company recognizes revenue when persuasive evidence of an arrangement exists, delivery has occurred, the price is fixed or determinable, risk of loss has passed to the customer and collection of the resulting receivable is reasonably assured. Revenue recognition requires judgment and estimates, which may affect the amount and timing of revenue recognized in any given period.

On January 1, 2011, the Company adopted the provisions of Accounting Standards Update (ASU) 2009-13, Revenue Recognition (Topic 605) Multiple-Deliverable Revenue Arrangements (ASU 2009-13). ASU 2009-13 addresses the accounting for multiple-element arrangements by providing two significant changes. First, this guidance removes the requirement to have objective and reliable evidence of fair value for undelivered elements in an arrangement and results in more elements being treated as separate units of accounting. Specifically, this guidance amends the criteria in Subtopic 605-25, Revenue Recognition-Multiple-Element Arrangements (ASC 605-25), for separating consideration in multiple-element arrangements. This guidance establishes a selling price hierarchy for determining the selling price of an element, which is based on: (a) vendor-specific objective evidence; (b) third-party evidence; or (c) management s best estimate. Management s best estimate for the Company was based on factors such as gross margin, volume discounts, new strategic customers, geography, customer class and competitive pressures. The second change modifies the manner in which the transaction consideration is allocated across the separately identified elements. Entities are no longer able to apply the residual method of allocation and instead the arrangement consideration is required to be allocated at the inception of the arrangement to all elements using the relative selling price method. The relative selling price method uses the weighted average of the selling price and applies that to the contract value to establish the consideration for each element.

For transactions entered into prior to the adoption of ASU 2009-13, the Company follows the provisions of ASC 605-25 for all multiple-element arrangements. Under the guidance prior to ASU 2009-13, the Company assesses whether the elements specified in a multiple-element arrangement should be treated as separate units of accounting for revenue recognition purposes and whether objective and reliable evidence of fair value exists for these separate units of accounting. The Company applies the residual method when objective and reliable evidence of fair value exists for all of the undelivered elements in a multiple-element arrangement. When objective and reliable evidence of fair value does not

exist for all of the undelivered elements in a multiple-element arrangement, the Company recognizes revenue under the multiple units shipped methodology, whereby revenue is recognized in each period based upon the lowest common percentage of the products shipped in the period. This approximates a proportional performance model of revenue recognition. This generally results in a partial deferral of revenue to a later reporting period. No revenue is recognized unless one or more units of each product have been delivered.

Table of Contents

On January 1, 2011, the Company adopted the provisions of ASU 2009-14, Software (Topic 985) Certain Revenue Arrangements That Include Software Elements (ASU 2009-14). ASU 2009-14 changes revenue recognition for tangible products containing software and hardware elements. Specifically, tangible products containing software and hardware that function together to deliver the tangible products essential functionality are scoped out of the existing software revenue recognition guidance and will be accounted for under the multiple-element arrangements revenue recognition guidance under ASU 2009-13. With the adoption of ASU 2009-14, the Company concluded that when there is software included in tangible products, it is essential to the functionality of the tangible product. It is therefore outside the scope of ASC 985-605, Software Revenue Recognition (ASC 985-605) as amended. Prior to the adoption of ASU 2009-14, although certain of the Company s products contain operating and application software, the Company had determined the software element was incidental in accordance with ASC 985-605.

Based on the guidance in ASC 985-605, multiple purchase orders may be deemed to be interrelated and considered to constitute a multiple-element arrangement for accounting purposes.

Semiconductor Systems transactions are generally multiple-element arrangements which may include hardware, software, installation, training, an initial standard warranty, and optional extended warranty arrangements. The Company generally designs, markets and sells these products as standard configurations. Typically, revenue is recorded at the time of shipment or acceptance, which is the same under pre and post-adoption of ASU 2009-13. Acceptance is generally required for sales of Semiconductor Systems segment products to Japanese customers and sales of New Products . New Products are considered by the Company, for purposes of revenue recognition determination, to be either (a) a product that is newly released to all customers, including a product which may have been existing previously, but which has been substantially upgraded with respect to its features or functionality; or, (b) the sale of an existing product to a customer who has not previously purchased that product. The Company follows a set of predetermined criteria when changing the classification of a New Product to a standard configuration whereby acceptance criteria are considered to be demonstrated at the time of shipment.

The Laser Products and Precision Motion and Technologies segments have revenue transactions that are comprised of both single-element and multiple-element transactions. Multiple-element transactions may include two or more products and occasionally also contain installation, training or preventative maintenance plans. For multiple-element transactions entered into or materially modified after January 1, 2011, revenue is recognized under ASU 2009-13, generally upon shipment using the relative selling price method. For all other multiple-element transactions, revenue is generally recognized under the multiple units shipped methodology described above. Single-element transactions are generally recognized upon shipment.

The Company s Semiconductor Systems segment also sells spare parts and consumable items, which are not subject to acceptance criteria. For multiple-element transactions entered into or materially modified after January 1, 2011, revenue is recognized under ASU 2009-13, generally upon shipment using the relative selling price method. For all other multiple-element transactions, revenue is generally recognized under the multiple units shipped methodology described above. Single-element transactions are generally recognized upon shipment.

Installation is generally a routine process that occurs within a short period of time from delivery and the Company has concluded that this obligation is inconsequential and perfunctory. As such, for transactions that include installation, and for which customer acceptance has not been deemed necessary in order to record the revenue, the cost of installation is accrued at the time product revenue is recorded and no related revenue is deferred. Historically, the costs of installation have not been significant.

The initial standard warranty for product sales is accounted for under the provisions of ASC 450, Contingencies , as the Company has the ability to ascertain the probable likelihood of the liability, and can estimate the amount of the liability. A provision for the estimated cost related to warranty is recorded to cost of goods sold at the time revenue is recognized. The Company s estimate of costs to service the warranty obligations are based on historical experience and expectations of future conditions. To the extent the Company experiences increased warranty claims or increased costs associated with servicing those claims, revisions to the estimated warranty liability are recorded as increases or decreases to the accrual at that time, with an offsetting entry recorded to cost of goods sold.

The Company also sells optional extended warranty services, and preventative maintenance contracts, at the time of their product purchase. The Company accounts for these agreements in accordance with provisions of ASC 605-20-25-3, Separately Priced Extended Warranty and Product Maintenance Contracts , under which it recognizes the separately priced extended warranty and preventative maintenance fees over the associated period.

The Company, at the request of its customers, may at times perform professional services for its customers, generally for the maintenance and repairs of products previously sold to those customers. These services are usually in the form of time and materials based contracts which are short in their duration. Revenue for time and material services is recorded at the

9

completion of services requested under a customer s purchase order. Customers may, at times subsequent to the initial product sale, purchase a service contract whereby services, including preventative maintenance plans, are provided over a defined period, generally one year. Revenue for such service contracts are recorded ratably over the period of the contract.

The Company typically negotiates trade discounts and agreed terms in advance of order acceptance and records any such items as a reduction of revenue. The Company s revenue recognition policy allows for revenue to be recognized under arrangements where the payment terms are 180 days or less, presuming all other revenue recognition criteria have been met. From time to time, based on the Company s review of customer creditworthiness and other factors, the Company may provide its customers with payment terms that exceed 180 days. To the extent all other revenue recognition criteria have been met, the Company recognizes revenue for these extended payment arrangements as the payments become due.

The Company has deferred revenue included in its accompanying consolidated balance sheets, with balances (including both current and long-term amounts) of $7.6 million and $15.4 million as of July 1, 2011 and December 31, 2010, respectively. The deferred revenue balance is primarily comprised of pre ASU 2009-13 multiple-element arrangements, delivered over multiple periods, whereby there is no fair value for one or more of the undelivered element(s) and arrangements where acceptance has not been received. To a much lesser extent, the deferred revenue balances relate to either: (a) the unrecognized portion of multiple-element arrangements that are being recognized into revenue ratably as associated services are performed; (b) arrangements not currently recognizable due to the arrangement not being fixed and determinable at its inception; (c) revenue deferrals for product shipments with FOB destination shipping terms; and (d) the future amortization of revenue related to extended warranty contracts and preventative maintenance plans. The classification of deferred revenue and deferred cost of goods sold is based on the Company s expectations with respect to when the revenue will be recognized, based on facts known to the Company as of the date its financial statements are released.

The Company had certain pre ASU 2009-13 multiple-element arrangements outstanding, delivered over multiple periods, in which the Company recognized $9.9 million and $26.2 million in revenue for the three and six months ended July 1, 2011, respectively. The $9.9 million includes $4.2 million of net revenue with net gross profit of $1.6 million resulting from the recognition of $4.6 million that had been deferred as of April 1, 2011, offset by $0.4 million of additional deferrals during the quarter from orders placed prior to January 1, 2011. The $26.2 million includes $6.4 million of net revenue with net gross profit of $2.8 million resulting from the recognition of $9.0 million that had previously been deferred, offset by $2.6 million of additional deferrals during the quarter from orders placed prior to January 1, 2011. As of July 1, 2011, the Company has $2.5 million in deferred revenue related to these arrangements, the majority of which is expected to be recognized throughout the remainder of 2011. Such arrangements will continue to be accounted for under the prior accounting standards until they are completed. For multiple-element arrangements, delivered over multiple periods, which were entered into after the adoption of ASU 2009-13, the Company recognized $13.3 million and $17.2 million in revenue for the three and six months ended July 1, 2011, respectively, with no deferrals related to the adoption of ASU 2009-13 as of July 1, 2011.

Accumulated Other Comprehensive Loss

The following table provides the details of accumulated other comprehensive loss at (in thousands):

	July 1, 2011	December 31, 2010
Foreign currency translation adjustments	$ 5,577	$ 2,568
Pension liability, net of tax	(5,846)	(5,997)
Total accumulated other comprehensive loss	$ (269)	$ (3,429)

Comprehensive Income (Loss)

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

	Three Months Ended		Six Months Ended	
	July 1, 2011	July 2, 2010	July 1, 2011	July 2, 2010

Consolidated net income (loss)	$ 10,075	$ (5,055)	$ 16,337	$ 986
Foreign currency translation adjustments (1)	784	(581)	3,009	(2,256)
Net reclassifications of investments, net of tax		(306)		(568)
Pension liability, net of tax	76	66	151	135
Consolidated comprehensive income (loss)	10,935	(5,876)	19,497	(1,703)
Less: Comprehensive income attributable to noncontrolling interest	(9)	(11)	(64)	(52)
Comprehensive income (loss) attributable to GSI Group Inc.	$ 10,926	$ (5,887)	$ 19,433	$ (1,755)

(1) The foreign currency translation adjustments are primarily related to the movement in the British Pound, Japanese Yen and European Union Euro.

Table of Contents

Net Income (Loss) Per Common Share

Basic net income (loss) attributable to GSI Group Inc. per common share is computed by dividing net income (loss) by the weighted-average number of common shares outstanding during the period. For diluted net income per common share, the denominator also includes any dilutive outstanding stock options, restricted stock awards and restricted stock units determined using the treasury stock method. Potentially dilutive securities are excluded from the diluted earnings per share computation to the extent they are anti-dilutive. Common and common share equivalent disclosures are (in thousands):

	Three Months Ended		Six Months Ended	
	July 1, 2011	July 2, 2010	July 1, 2011	July 2, 2010
Weighted average common shares outstanding - basic	33,478	15,967	33,464	15,960
Dilutive potential common shares (1)	117		100	21
Weighted average common shares outstanding - diluted	33,595	15,967	33,564	15,981
Excluded from diluted common shares calculation - weighted stock options, restricted stock awards and restricted stock units that are anti-dilutive	117	266	85	278

(1) Due to the Company s net loss position for the three months ended July 2, 2010, all potentially dilutive shares are excluded as their effect would have been anti-dilutive.

Recent Accounting Pronouncements

Recently Adopted Accounting Pronouncements

On January 1, 2011, the Company adopted ASU 2009-13, Multiple-Deliverable Revenue Arrangements and ASU 2009-14, Certain Revenue Arrangements that Include Software Elements . The impact of the Company s adoption of these pronouncements is discussed in the revenue recognition policy within this Note 3 to Consolidated Financial Statements.

Recently Issued Accounting Pronouncements

In June 2011, the Financial Accounting Standards Board (FASB) amended ASC 220, Presentation of Comprehensive Income. This amendment will require companies to present the components of net income and other comprehensive income either as one continuous statement or as two consecutive statements. It eliminates the option to present components of other comprehensive income as part of the statement of changes in stockholders equity. The amended guidance, which must be applied retroactively, is effective for interim and annual periods beginning after December 15, 2011, with earlier adoption permitted. This ASU impacts presentation only and will have no effect on our financial condition, results of operations or cash flows.

In May 2011, the FASB amended ASC 820, Fair Value Measurement. This amendment is intended to result in convergence between U.S. GAAP and International Financial Reporting Standards (IFRS) requirements for measurement of and disclosures about fair value. This guidance clarifies the application of existing fair value measurements and disclosures, and changes certain principles or requirements for fair value measurements and disclosures. The amendment is effective for interim and annual periods beginning after December 15, 2011. The adoption of this amendment will not have a material impact on our consolidated financial statements.

Table of Contents

4. Fair Value Measurements

The Company applies the guidance in ASC 820, which defines fair value, establishes a framework for measuring fair value, and specifies disclosures about fair value measurements. Fair value is defined as the price that would be received for an asset, or paid to transfer a liability, in an orderly transaction between market participants at the measurement date. Valuation techniques must maximize the use of observable inputs and minimize the use of unobservable inputs.

ASC 820 establishes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the third is considered unobservable:

Level 1. Quoted prices for identical assets or liabilities in active markets which the Company can access.

Level 2. Observable inputs other than those described in Level 1.

Level 3. Unobservable inputs.

The fair values of cash, accounts receivable, income taxes receivable, accounts payable, income taxes payable, accrued compensation and benefits, and other accrued expenses, approximate their carrying values because of their short-term nature. Cash equivalents, primarily money market accounts, represent the only asset the Company measures at fair value on a recurring basis. Cash equivalents of $5.7 million and $7.8 million as of July 1, 2011 and December 31, 2010, respectively, are classified as Level 1 in the fair value hierarchy because they are valued at quoted prices in active markets.

The Company conducted nonrecurring fair value measurements for the annual impairment tests for goodwill and intangible assets as of the beginning of the second quarter of 2011 and 2010, and determined that goodwill and intangible assets were not impaired.

See Note 7 to Consolidated Financial Statements for discussion of the estimated fair value of the Company s debt instruments.

5. Goodwill and Intangible Assets

Goodwill

Goodwill is recorded when the consideration for an acquisition exceeds the fair value of net tangible and identifiable intangible assets acquired. There were no changes in the carrying amount of goodwill during the three or six months ended July 1, 2011. Goodwill by reportable segment as of July 1, 2011 and December 31, 2010 is as follows (in thousands):

	Reportable Segment		
	Laser Products	**Precision Motion and Technologies**	**Total**
Goodwill	$ 67,926	$ 108,306	$ 176,232
Accumulated impairment of goodwill	(54,099)	(77,555)	(131,654)
	$ 13,827	$ 30,751	$ 44,578

Intangible Assets

As of July 1, 2011, intangible assets consisted of the following (in thousands):

	July 1, 2011			
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Weighted Average Remaining Life (Years)
Amortizable intangible assets:				
Patents and acquired technology	$ 61,580	$ (45,748)	$ 15,832	5.1
Customer relationships	33,215	(15,446)	17,769	8.0
Customer backlog	2,355	(2,355)		
Non-compete agreements	4,870	(4,659)	211	0.2
Trademarks, trade names and other	5,760	(3,330)	2,430	7.7
Amortizable intangible assets	107,780	(71,538)	36,242	6.7
Non-amortizable intangible assets:				
Trade names	13,027		13,027	
Totals	$ 120,807	$ (71,538)	$ 49,269	

Table of Contents

As of December 31, 2010, intangible assets consisted of the following (in thousands):

	December 31, 2010			
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Weighted Average Remaining Life (Years)
Amortizable intangible assets:				
Patents and acquired technology	$ 61,298	$ (43,546)	$ 17,752	5.5
Customer relationships	33,121	(14,183)	18,938	8.4
Customer backlog	2,355	(2,355)		
Non-compete agreements	4,870	(4,001)	869	0.7
Trademarks, trade names and other	5,696	(3,143)	2,553	8.2
Amortizable intangible assets	107,340	(67,228)	40,112	6.9
Non-amortizable intangible assets:				
Trade names	13,027		13,027	
Totals	$ 120,367	$ (67,228)	$ 53,139	

All definite-lived intangible assets are amortized on a straight-line basis over their remaining life. Amortization expense for customer relationships, customer backlog, non-compete agreements and definite-lived trademarks, trade names and other is included in operating expenses in the accompanying consolidated statements of operations and was $1.0 million and $1.1 million for the three months ended July 1, 2011 and July 2, 2010, respectively, and $2.0 million and $2.3 million for the six months ended July 1, 2011 and July 2, 2010, respectively. Amortization expense for the patents and acquired technology is included in cost of goods sold in the accompanying consolidated statements of operations and was $1.0 million for each of the three months ended July 1, 2011 and July 2, 2010, and $2.0 million and $1.9 million, respectively, for the six months ended July 1, 2011 and July 2, 2010.

Estimated amortization expense for each succeeding period after July 1, 2011 is as follows (in thousands):

Year Ending December 31,	Cost of Goods Sold	Operating Expenses	Total
2011 (6 months from July 1, 2011)	$ 1,903	$ 1,537	$ 3,440
2012	3,165	2,652	5,817
2013	3,165	2,652	5,817
2014	3,165	2,565	5,730
2015	2,065	2,395	4,460
Thereafter	2,369	8,609	10,978
Total	$ 15,832	$ 20,410	$ 36,242

6. Supplementary Balance Sheet Information

The following tables provide the details of selected balance sheet items as of the periods indicated:

Inventories

	July 1, 2011	December 31, 2010
	(In thousands)	
Raw materials	$ 37,888	$ 37,315
Work-in-process	18,060	16,613
Finished goods	11,568	10,261
Demo inventory	2,379	1,249
Consigned inventory	1,217	1,283
Total inventories	$ 71,112	$ 66,721

Table of Contents

Prepaid Expenses and Other Current Assets

	July 1, 2011	December 31, 2010
	(In thousands)	
Prepaid expenses	$ 4,869	$ 4,803
Other current assets	1,256	777
Total	$ 6,125	$ 5,580

Other Accrued Expenses

	July 1, 2011	December 31, 2010
	(In thousands)	
Accrued interest	$ 1,655	$ 1,647
Accrued warranty	3,715	3,977
Accrued professional fees	1,460	2,165
Accrued third party sales commissions	554	497
Customer deposits	2,442	1,241
Accrued restructuring, current portion	983	797
Deferred rent, current portion	1,325	1,325
Accrued VAT	238	540
Other	2,410	2,528
Total	$ 14,782	$ 14,717

Accrued Warranty

	Six Months Ended	
	July 1, 2011	July 2, 2010
	(In thousands)	
Balance at beginning of period	$ 3,977	$ 3,140
Charged to costs and expenses	1,382	2,466
Use of provision	(1,723)	(1,965)
Foreign currency exchange rate changes	79	(82)
Balance at end of period	$ 3,715	$ 3,559

Other Liabilities

	July 1, 2011	December 31, 2010

	(In thousands)	
Deferred rent	$ 1,490	$ 2,151
Accrued PIK		269
Total	$ 1,490	$ 2,420

7. Debt

12.25% Senior Secured PIK Election Notes

Upon the emergence from bankruptcy, GSI US issued $107.0 million in aggregate principal amount of 12.25% Senior Secured PIK Election Notes, which mature on July 23, 2014 (the New Notes), pursuant to that certain Indenture (the New Indenture), by and among GSI US, as issuer, the Guarantors named therein (including GSIG and MES) and The Bank of New York Mellon Trust Company, N.A., as trustee.

Interest accrues on the New Notes at a rate of 12.25% per year and is payable quarterly in arrears on February 15, May 15, August 15 and November 15 of each year, commencing on August 15, 2010. GSI US may elect to pay the interest in cash, or, under certain conditions, by increasing the principal amount of the New Notes or issuing additional notes on the same terms and conditions as the existing New Notes (PIK). However, the Company is required to pay cash interest if its fixed charge coverage ratio is greater than 1.75 to 1.00. Furthermore, until the Company became current in its reporting obligations under the Securities Exchange Act of 1934, as amended (the Exchange Act) and until the Company s common shares were listed on an Eligible Market (as defined in the New Indenture), the rate of interest under the New Notes was increased by an additional 2% per annum (Default Rate), payable by PIK beginning after August 15, 2010. Additionally, the interest rate on the New Notes may be increased under certain defaults, as defined in the New Indenture. Interest PIK notes issued and PIK payments in lieu of cash payments accrue interest at a rate of 13% per annum. The Company became current in its reporting obligations under the Exchange Act on December 13, 2010 with the filing of its Form 10-Q for the quarter-ended October 1, 2010. On February 14, 2011, the Company s common shares were listed on The NASDAQ Global Select Market under the trading symbol GSIG . Accordingly, as of February 14, 2011, the 2% per annum additional interest penalty ceased. PIK notes issued to noteholders as a result of the 2% penalty from August 15, 2010 to February 14, 2011 totaled $1.1 million and are classified as debt in the accompanying balance sheet as of July 1, 2011.

On July 18, 2011, GSI US provided formal notice that it had elected to optionally redeem $35.0 million in aggregate principal amount (constituting 32% of the currently outstanding $108.1 million in aggregate principal amount) of its outstanding New Notes, including PIK notes, in accordance with the terms of the New Indenture, pursuant to which the New Notes were issued. In accordance with the New Indenture, the redemption price for the New Notes being redeemed will be 100% of the principal amount of such New Notes, plus accrued and unpaid interest thereon, if any, to, but not including, August 17, 2011, the redemption date. After consummation of this redemption, $73.1 million in aggregate principal amount of the New Notes, including PIK notes, will remain outstanding. The redemption will be financed from a portion of the available cash and cash equivalents of the Company and its subsidiaries.

Interest expense on the New Notes for the three and six months ended July 1, 2011 was $3.4 million and $7.1 million, respectively, including PIK interest of $0.3 million during the six months ended July 1, 2011. The PIK interest relates to the additional 2% assessment per annum as described above, which ceased in February 2011. As of July 1, 2011, accrued interest totaled $1.7 million, which is classified as other accrued expenses in the accompanying consolidated balance sheet as of July 1, 2011. A $0.5 million PIK note was issued in February 2011 and is classified as debt in the accompanying consolidated balance sheet as of July 1, 2011. The Company recorded interest expense of $5.7 million and $11.5 million for the three and six months ended July 2, 2010, respectively, related to the $210.0 million of 11% unsecured senior notes due 2013 (the 2008 Senior Notes), which were restructured upon bankruptcy emergence, as described in Note 2 and Note 8 to the Consolidated Financial Statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2010, filed with the SEC on March 30, 2011.

Deferred Financing Costs

In connection with the issuance of the New Notes, the Company capitalized $1.6 million in deferred financing costs, which are included in other assets in the accompanying consolidated balance sheet as of July 1, 2011. These deferred financing costs are being amortized to interest expense on a straight-line basis over the four year contractual term of the New Notes. As of July 1, 2011, the unamortized portion of the deferred financing costs was $1.2 million. Non-cash interest expense related to the amortization of the deferred financing costs for the three and six months ended July 1, 2011 was $0.1 million and $0.2 million, respectively.

Guarantees

Each Guarantor, as defined in the New Indenture, jointly and severally, unconditionally guarantees (each a Note Guarantee and collectively the Note Guarantees) the due and punctual payment of the principal of and interest on the New Notes, when due and payable, whether at maturity, by acceleration or otherwise, the due and punctual payment of interest on the overdue principal of and interest on the New Notes, the due and punctual payment of all other Obligations, as defined in the New Indenture, and the due and punctual performance of all obligations of the Company in accordance with the terms of the New Indenture. Furthermore, each Guarantor, as defined in the New Indenture, jointly and severally, unconditionally guarantees that in the event of any extension of time of payment or renewal of any of the New Notes or any of such other Obligations, as defined in the New Indenture, with respect to the New Notes, amounts due will be promptly paid in full when due or performed in accordance with the terms of the extension or renewal, at stated maturity, by acceleration or otherwise. Further discussion of the Note Guarantees is provided in Note 8 to the Consolidated Financial Statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2010, filed with the SEC on March 30, 2011.

As of July 1, 2011, the maximum potential amount of future payments the Guarantors could be required to make under the Note Guarantees is the principal amount of the New Notes plus all unpaid, but accrued interest thereon, including all PIK and Default Rate interest. However, as of July 1, 2011, the Guarantors are not expected to be required to perform under the Note Guarantees.

Fair Value of Debt

The Company emerged from bankruptcy with $107.0 million of 12.25% Senior Secured PIK Election Notes, plus an additional $1.1 million of PIK notes, issued from August 15, 2010 to February 14, 2011, which mature on July 23, 2014. Since the date the New Notes were issued, trading activity with respect to New Notes has been limited. As of July 1, 2011, the estimated fair value of the Company s New Notes approximated $120.0 million. As of December 31, 2010, the estimated fair value of the Company s New Notes approximated $113.4 million. These fair value estimates represent the value at which the Company estimates the lenders could trade the debt within the financial markets, and does not represent the settlement value of these long-term debt liabilities to the Company. The fair value of the New Notes will continue to fluctuate each period and these fluctuations may have little to no correlation to the Company s outstanding debt balances. The Company estimated the appropriate market yield for the New Notes based on yields for comparable issues and market indices. Using this market yield, the Company calculated the present value of future interest and principal payments to estimate the fair value of the New Notes. Fair value estimates are made at a specific point in time based on relevant market information. These estimates are subjective in nature and involve uncertainties and matters of significant judgments and therefore cannot be determined with precision. Changes in market conditions, valuation assumptions or approach could significantly affect these estimates.

8. Share-Based Compensation

Equity Compensation Plans

As of July 1, 2011, the Company has one active equity compensation plan, the GSI Group Inc. 2010 Incentive Award Plan (the 2010 Incentive Plan), under which it may grant stock-based compensation awards to employees, consultants and directors. As of July 1, 2011, there are 2,092,659 shares available for future issuance under the 2010 Incentive Plan. Additionally, the Company has other equity compensation plans under which there are awards outstanding, but under which no further awards may be made as such plans were cancelled upon the Company s emergence from bankruptcy on July 23, 2010 (collectively referred to herein as the Pre-2010 Incentive Plans). Such equity compensation plans are described in Note 10 in the Notes to Consolidated Financial Statements included in the Company s Annual Report on Form 10-K for the year-ended December 31, 2010, filed with the SEC on March 30, 2011. There have been no material modifications made to the Company s equity compensation plans during the three or six months ended July 1, 2011.

2010 Incentive Plan

The table below summarizes activity relating to restricted stock units issued and outstanding under the 2010 Incentive Plan during the six months ended July 1, 2011:

	Number of Shares (In thousands)	Weighted Average Grant Date Fair Value
Unvested at December 31, 2010	333	$ 9.87
Granted	435	11.62
Vested		
Forfeited	(5)	10.30
Unvested at July 1, 2011	763	$ 10.86
Expected to vest as of July 1, 2011	760	$ 10.87

Pre-2010 Incentive Plans

The table below summarizes activity relating to restricted stock awards issued and outstanding under the Pre-2010 Incentive Plans during the six months ended July 1, 2011:

	Number of Shares (In thousands)	Weighted Average Grant Date Fair Value
Unvested at December 31, 2010	31	$ 11.36
Granted		
Vested	(10)	24.30
Forfeited	(6)	8.12
Unvested at July 1, 2011	15	$ 3.84

Table of Contents

Share-Based Compensation Expense

The Company recognized share-based compensation expense totaling $0.8 million and $0.4 million during the three months ended July 1, 2011 and July 2, 2010, respectively, and $1.8 million and $1.1 million during the six months ended July 1, 2011 and July 2, 2010, respectively. Stock compensation expense is primarily included in selling, general, and administrative expense in the Company s consolidated statements of operations and as an increase to additional paid-in capital on the Company s consolidated balance sheets. As the awards granted are issuable to the holder, typically subject to vesting provisions, with no consideration payable by the holder, the grant date fair value per share is based on the quoted price of the Company s common stock on the date of the grant and is generally the basis for which compensation expense is recognized. The restricted stock awards and restricted stock units for which the Company has recorded expense during the three and six months ended July 1, 2011 and July 2, 2010, have generally been issued with a three-year vesting period and vest based solely on service conditions. Accordingly, the Company recognizes compensation expense on a straight-line basis over the requisite service period. The Company reduces the compensation expense by an estimated forfeiture rate which is based on anticipated forfeitures and actual experience.

Additionally, the expense recorded during the six months ended July 1, 2011 includes compensation expense for 42,536 deferred stock units granted to the members of the Company s Board of Directors, pursuant to the Company s 2010 Incentive Plan, of approximately $0.6 million, which was recognized in full on the date of grant, as the deferred stock units are fully vested and nonforfeitable on the date of grant. There were no deferred stock units granted during the three months ended July 1, 2011 or the three or six months ended July 2, 2010. Approximately $0.1 million and $0.4 million of the compensation expense recognized during the three and six month periods ended July 1, 2011 and July 2, 2010, respectively, relates to expense recognized upon the acceleration of vesting of all outstanding but unvested restricted stock awards or units that had previously been granted to certain of the Company s former executives as of the respective effective dates of termination. The expense recorded during the three and six months ended July 2, 2010 includes ($0.1) million and $0.2 million, respectively, of compensation expense related to awards granted under the Pre-2010 Incentive Plans that were accounted for as share-based liabilities under ASC 718, Stock Compensation , until settled through the issuance of common shares, forfeited due to termination of service or reclassified to additional paid in capital, upon the Company s emergence from bankruptcy on July 23, 2010. Accordingly, no share-based liability remains as of July 1, 2011 or December 31, 2010. No awards were accounted for as share-based liabilities during the three or six months ended July 1, 2011.

As of July 1, 2011, there was $7.2 million of unrecognized compensation related to unvested restricted stock units and unvested restricted stock awards. This amount is expected to be recognized over a weighted-average period of 2.6 years. To the extent the actual forfeiture rate is different from what the Company has anticipated, the share-based compensation expense related to these awards will differ from these expectations.

9. Employee Benefit Plans

U.K. Defined Benefit Pension Plan

The net periodic pension cost for the U.K defined benefit pension plan includes the following components (in thousands):

	Three Months Ended		Six Months Ended	
	July 1, 2011	July 2, 2010	July 1, 2011	July 2, 2010
Components of the net periodic pension cost:				
Interest cost	$ 382	$ 351	$ 757	$ 724
Expected return on plan assets	(398)	(339)	(789)	(699)
Amortization of loss	57	49	113	101
Net periodic pension cost	$ 41	$ 61	$ 81	$ 126

Table of Contents

Japan Defined Benefit Pension Plan

The net periodic pension cost for the Japan defined benefit pension plan includes the following components (in thousands):

	Three Months Ended		Six Months Ended	
	July 1, 2011	**July 2, 2010**	**July 1, 2011**	**July 2, 2010**
Components of the net periodic pension cost:				
Service cost	$ 51	$ 46	$ 101	$ 93
Interest cost	7	6	14	12
Amortization of unrecognized transition obligation	19	17	38	34
Net periodic pension cost	$ 77	$ 69	$	