

GSI GROUP INC  
Form 10-K  
April 13, 2010  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-K**

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

For the fiscal year ended December 31, 2008

OR

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

Commission File No. 000-25705

**GSI Group Inc.**

(Exact name of registrant as specified in its charter)

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<b>New Brunswick, Canada</b> (State or other jurisdiction of incorporation or organization)	<b>98-0110412</b> (I.R.S. Employer Identification No.)
<b>125 Middlesex Turnpike</b> <b>Bedford, Massachusetts, USA</b> (Address of principal executive offices)	<b>01730</b> (Zip Code)
<b>(781) 266-5700</b>	
(Registrant's telephone number, including area code)	

**Securities Registered Pursuant to Section 12(b) of the Act:**

<b>Title of Class</b>	<b>Name of Exchange on which Registered</b>
<b>Common Shares, no par value</b>	<b>NASDAQ</b>

**Securities Registered Pursuant to Section 12(g) of the Act:**

**None**

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

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, 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  No

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

Large accelerated filer  Accelerated filer

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

The aggregate market value of the Registrant's outstanding common shares held by non-affiliates of the Registrant, based on the closing price of the common shares on The NASDAQ Stock Market on the last business day of the Registrant's most recently completed second fiscal quarter (June 27, 2008) was approximately \$150,504,163. For purposes of this disclosure, common shares held by officers and directors of the Registrant and by persons who hold more than 5% of the Registrant's outstanding common shares have been excluded because such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily conclusive.

There were approximately 47,901,978 of the Registrant's common shares, no par value, issued and outstanding on March 23, 2010.

### **DOCUMENTS INCORPORATED BY REFERENCE.**

None.

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**GSI GROUP INC.**

**FORM 10-K**

**YEAR ENDED DECEMBER 31, 2008**

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As used in this report, the terms we, us, our, GSI Group, GSI, GSIG and the Company mean GSI Group Inc. and its subsidiaries, unless context indicates another meaning.

Unless otherwise noted, all dollar amounts in this report are expressed in United States dollars.

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The following trademarks and trade names of GSI Group are used in this report: WaferMark , WaferRepair , WaferTrim , CircuitTrim , SVS , MicroE<sup>®</sup> and Westwind.

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**EXPLANATORY NOTE**

In August 2008, GSI Group Inc. (the Company) closed its acquisition of Excel Technology, Inc. (Excel). Delays in the integration of the financial accounting systems of the Company and Excel following the acquisition initially led to a delay of several weeks in the preparation of the Company's Quarterly Report on Form 10-Q for the quarterly period ended September 26, 2008 (the 2008 Q3 Report). Shortly thereafter and prior to filing the 2008 Q3 Report, the Company initiated an internal review of certain potential errors in the recognition of revenue related to sales to a customer in the first and second fiscal quarters of 2008 in the Company's Semiconductor Systems Segment, which were brought to the attention of the Audit Committee of the Company's Board of Directors (the Audit Committee) by Company management. Following this initial internal review, the Audit Committee, in consultation with the Company's outside legal counsel determined that it was appropriate to undertake an independent review of the potential revenue recognition issues brought to its attention.

On or about November 25, 2008, the Audit Committee initiated a broader independent review of sales transactions in the Semiconductor Systems Segment that contain arrangements with multiple deliverables for fiscal years 2007 and 2008. The review was subsequently expanded to include sales transactions in the Semiconductor Systems Segment, along with certain other sales transactions for fiscal years 2006, 2007 and 2008. To assist in its review, the Audit Committee retained independent legal counsel and forensic accounting experts.

On December 4, 2008, the Company announced that it identified errors in the recognition of revenue related to sales to a customer in the first and second fiscal quarters of 2008 in the Semiconductor Systems Segment and that the previously issued financial statements contained in the Company's Quarterly Reports on Form 10-Q for the periods ended March 28, 2008 and June 27, 2008 should no longer be relied upon.

Subsequently, the Company announced that it had identified additional revenue recognition errors related to the timing of revenue recognition from sales to certain Semiconductor Systems Segment customers during fiscal year 2007. The Audit Committee concluded, upon the recommendation of Company management, that the range of potential adjustments resulting from the identified errors is material to the financial statements of the Company for the periods indicated and as a result, the Audit Committee determined that the previously issued interim and annual historical financial statements for 2007 should no longer be relied upon. The Audit Committee thereafter expanded the scope of its investigation to include fiscal year 2006.

On March 30, 2009, the Company announced that it had identified additional revenue recognition errors related to the timing of revenue recognition from sales to certain Semiconductor Systems Segment customers during fiscal year 2006. The Audit Committee concluded, upon the recommendation of Company management, that the range of potential adjustments resulting from the identified errors is material to the financial statements of the Company for the periods indicated and as a result, the Audit Committee determined that the previously issued interim and annual historical financial statements for 2006 should no longer be relied upon.

The Audit Committee's advisors reported the results of the investigation to the Audit Committee on April 24, 2009. The Company voluntarily reported the investigation results to the Securities and Exchange Commission (SEC) on April 30, 2009. The Company later announced in May 2009 that it was reviewing sales transactions of its Semiconductor Systems Segment during fiscal years 2004 and 2005 to determine if adjustments needed to be made to those periods. Thereafter, on June 30, 2009, the Company announced that it was undertaking a preliminary review of the timing of revenue recognized in connection with multiple element arrangements in its Precision Technology Segment from 2004 through 2008 to determine if adjustments need to be made to those periods (collectively with the Audit Committee's review of transactions in the Semiconductor Systems Segment and any other related Company reviews of transactions in the Semiconductor Systems Segment and Precision Technology Segment, the Revenue Review). As is further explained in Note 2 of the Notes to Consolidated Financial Statements, in connection with the Revenue Review, the Company concluded that there were a number of adjustments required that primarily relate to revenue recognition and the corresponding adjustments to deferred revenue, cost of goods sold and other assets. Adjustments to revenue resulted in revenue and their related costs being deferred and recognized in subsequent periods once all revenue recognition criteria have been met. In addition, these adjustments did not affect the Company's cash balances. The transactions that are being restated as a result of the Revenue Review include transactions for which the complete facts required to make the appropriate assessment with respect to the timing of the revenue recognition were not communicated to the finance department at the time the initial revenue was booked. As of December 31, 2008, a substantial portion of the revenue deferred through the restatement remains deferred, pending the finalization of all deliverables under the terms of the arrangements with customers. The revenue adjustments, in aggregate for both the Semiconductor Systems and the Precision Technology Segments, primarily relate to:

multiple-element arrangements for which objective and reliable evidence of fair value does not exist for one or more of the undelivered elements;



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for those arrangements whereby it was determined that customer acceptance was required in order to record revenue in accordance with the Company's policy, the correction of the timing of revenue for instances where customer acceptance could not be demonstrated until a period subsequent to the period of original revenue recognition;

contractual terms that resulted in arrangements being deemed to not be fixed or determinable at the outset of the arrangement (including extended payment terms and contracts whereby product quantity mix was subject to adjustment during the term of the arrangement); and

certain other revenue adjustments which were not individually, or in the aggregate, significant. These adjustments have been reflected in the restated consolidated financial statements and primarily relate to the accounting for separately priced extended warranty contracts.

In addition to adjustments from the Revenue Review, the Company has also identified and recorded the impact of certain adjustments which, due to their materiality, were not previously recorded. Certain of these adjustments affect revenue, cost of goods sold and operating expenses, as well as offsetting balance sheet accounts. These adjustments have been reflected in the accompanying consolidated financial statements.

In connection with its restatement, the Company and Ernst & Young LLP, its independent auditors, identified and reported to the Company's Audit Committee significant internal control matters that collectively constitute material weaknesses. Please see Item 9A. Controls and Procedures below for a description of these matters, and of certain of the measures that have been implemented during 2009, to date, as well as additional steps the Company plans to take to strengthen its controls.

The Company does not anticipate amending its previously filed annual reports on Form 10-K or any quarterly reports on Form 10-Q. The consolidated financial statements and related consolidated financial information contained in previously filed reports, including for the years ended December 31, 2007 and 2006 and for the first two quarterly reports during 2008 and the first three quarters of 2007, should no longer be relied upon. See Note 17 of the Notes to Consolidated Financial Statements for disclosure of quarterly results of operations for each quarter in 2007 and 2008.



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**PART I**

**Cautionary Note Regarding Forward-Looking Statements**

Except for historical information, the matters discussed in this Annual Report on Form 10-K are forward looking statements that involve risks, uncertainties and assumptions that, if they never materialize or if they prove incorrect, could cause our consolidated results to differ materially from those expressed or implied by such forward-looking statements. The Company makes such forward-looking statements under the provision of the Safe Harbor section of the Private Securities Litigation Reform Act of 1995. Actual future results may vary materially from those projected, anticipated, or indicated in any forward-looking statements as a result of various factors, including those set forth in Item 1A of this Annual Report on Form 10-K under the heading Risk Factors. Readers should also carefully review the risk factors described in the other documents that the Company files from time to time with the SEC. In this Annual Report on Form 10-K, the words anticipates, believes, expects, intends, future, could, estimates, plans, will, could, would, should, potential, continues and similar words or expressions (and other words or expressions referencing future events, conditions or circumstances) identify forward-looking statements. Forward-looking statements also include the assumptions underlying or relating to any of the foregoing statements. The forward-looking statements contained in this Annual Report include, without limitation, statements about our reorganization proceedings under Chapter 11 of the U.S. Bankruptcy Code, our ability to continue as a going concern, the value of our common shares, our delisting proceedings with NASDAQ, our internal controls over our accounting for revenue recognition and income tax transactions, our internal controls over our financial close process, our results of operations and our financial condition. All forward-looking statements included in this document are based on information available to us on the date hereof. We will not undertake and specifically decline any obligation to update any forward-looking statements.

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### **Item 1. Business OVERVIEW**

GSI Group Inc. and its subsidiaries (collectively referred to as the Company) design, develop, manufacture and sell photonics-based solutions (consisting of lasers, laser systems and electro-optical components), precision motion devices, associated precision motion control technology and systems. Its customers incorporate its technology into their products or manufacturing processes, for a wide range of applications in a variety of markets, including: industrial, scientific, electronics, semiconductor, medical 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's products are grouped into three segments: Precision Technology, Semiconductor Systems and Excel Technology, Inc. (Excel). The Company strives to create shareholder value through:

Organic sales growth by delivering a consistent stream of successful new product launches,

Generating high levels of cash flow from operations, and

Acquiring and successfully integrating businesses that have complementary and established core competencies.

GSI Group Inc., founded in 1968 as General Scanning, Inc., was initially incorporated in Massachusetts. General Scanning developed, manufactured and sold components and subsystems for high-speed micro positioning of laser beams. In 1999 General Scanning merged with Lumonics Inc., a Canadian company that developed, manufactured and sold laser-based, advanced manufacturing systems for electronics, semiconductor, and general industrial applications. GSI Lumonics Inc., the post-merger entity, continued under the laws of the Province of New Brunswick, Canada. In 2005, the Company renamed itself GSI Group Inc.

In addition to the restatement of the Company's financial results, which is discussed in the preceding Explanatory Note and further described in detail in Note 2 of Notes to Consolidated Financial Statements, a number of significant events have occurred since August 2008 and through the filing of this Annual Report on Form 10-K. Each of these recent events is discussed below. Following the discussion of these recent events is a discussion of the Company's continuing operations.

### ***SIGNIFICANT RECENT EVENTS***

#### *Acquisition of Excel Technology, Inc. in August 2008*

In August 2008, the Company acquired Excel, a designer, manufacturer and marketer of photonics-based solutions consisting of lasers, laser-based systems, precision motion devices and electro-optical components, primarily for industrial and scientific applications. Excel, which was headquartered in East Setauket, New York, manufactures its products in plants located in the United States and Germany, and sells its products to customers worldwide, both directly and indirectly through resellers and distributors. The Company acquired Excel in exchange for a cash payment of \$368.7 million, including transaction costs, a portion of which was financed by entering into a loan agreement for \$210.0 million. This loan is further discussed in the section below titled Chapter 11 Bankruptcy Filing, and in Note 8 of Notes to Consolidated Financial Statements. Subsequent to the acquisition of Excel, the Company established a third segment which is comprised solely of the operations of the newly acquired entity. See Note 4 of Notes to Consolidated Financial Statements for further details regarding the Excel transaction.

#### *Divestiture of General Optics Business in October 2008*

On October 8, 2008, the Company completed the sale of its General Optics business, located in Moorpark, California, (the U.S. Optics Business) for a sale price of \$21.6 million, which represented a gain of \$8.7 million, net of tax. The sale of the U.S. Optics Business is reported as Gain on Disposal of Discontinued Operations in our consolidated statements of operations for the year ended December 31, 2008. This business was part of the Company's Precision Technology Segment. The results of operations of the U.S. Optics Business have been reclassified and reported as income from discontinued operations in our consolidated statements of operations. See Note 5 of Notes to Consolidated Financial Statements for further details regarding the sale of the U.S. Optics Business.



**Table of Contents***NASDAQ Delisting Determination*

On November 3, 2009, the NASDAQ Hearing Panel (the Panel) of the NASDAQ Stock Market (NASDAQ) notified the Company that it had determined to delist the Company's common shares from the NASDAQ Global Select Market and to suspend trading in the Company's common shares effective at the open of market on November 5, 2009. The Panel's determination was made in connection with the Company's non-compliance with the filing requirements set forth in Listing Rule 5250(c)(1) due to the delayed filing of certain of our periodic reports. As permitted by NASDAQ rules, the Company timely appealed the Panel's determination to the NASDAQ Listing and Hearing Review Council (the Listing Council). On January 15, 2010, the Listing Council notified the Company that it affirmed the Panel's decision to delist the Company's securities. On March 15, 2010, the Company received notification from the NASDAQ Stock Market, LLC Board of Directors (the NASDAQ Board) that the NASDAQ Board has declined to call for review the January 15, 2010 decision of the Listing Council. Accordingly, pursuant to Listing Rule 5825, the Listing Council's decision represents the final decision of NASDAQ. In accordance with Listing Rule 5830 and Rule 12d2-2 under the Securities Exchange Act of 1934, NASDAQ filed an application on Form 25 with the SEC on April 5, 2010, to delist the Company's securities from NASDAQ. The application will become effective ten days after filing.

The Company's common shares are currently quoted on the Pink OTC Markets Inc., continuing under the trading symbol GSIGQ. The Company intends to seek relisting of its common shares on a national exchange as soon as possible once it becomes current in its reporting obligations.

*Chapter 11 Bankruptcy Filing*

In connection with the Company's failure to file the 2008 Q3 Report, as described in the Explanatory Note, on December 12, 2008, the Company announced that it had received four letters from certain noteholders of the 11% Senior Notes due in 2013, in the principal amount of \$210.0 million (the Senior Notes), issued by GSI Group Corporation (GSI US), alleging that the Company had failed to comply with a covenant in the Senior Note Indenture (the Indenture), relating to the Senior Notes, as a result of the Company's failure to file its 2008 Q3 Report within the time period specified by the rules and regulations of the SEC. These noteholders further alleged that, if such failure continued for 60 days from the date that the Company received notices of failure from holders comprising at least 25% of the aggregate principal amount of Senior Notes then outstanding, then such failure would constitute an event of default. Although the Company asserted that the letters did not constitute proper notice as required pursuant to the terms of the Indenture, and notified the trustee under the Indenture as such, the Company continued to work diligently to complete the review by its Audit Committee and to file its 2008 Q3 Report to avoid any claim of an Event of Default from occurring under the Indenture. Upon receipt of the letters from the noteholders, the Company commenced discussions with certain of the noteholders. On February 11, 2009, the Company announced that it entered into forbearance agreements with certain noteholders holding greater than 75% of the outstanding aggregate principal amount of the Senior Notes, pursuant to which such noteholders agreed to forebear from taking any action or exercising any remedies under the Indenture as a result of the Company's delayed periodic reports until February 27, 2009, pursuant to other terms and conditions more specifically set forth therein. On June 30, 2009, the Company announced that it reached an agreement on a non-binding term sheet with certain noteholders to consensually restructure the Company's outstanding obligations under the Senior Notes.

Following negotiations between the Company and certain noteholders about the restructuring, on November 20, 2009 (the Petition Date), GSI Group Inc. (GSIG) and two of its United States subsidiaries, GSI US and MES International, Inc. (MES and, collectively with GSIG and GSI US, the Debtors), filed voluntary petitions for relief (the Chapter 11 Petitions) under Chapter 11 of the United States Bankruptcy Code (the Bankruptcy Code) in the United States Bankruptcy Court for the District of Delaware (the Court) (the Chapter 11 Cases). Following the Petition Date, the Debtors will continue to operate their business as debtors-in-possession under the jurisdiction of the Court and in accordance with the applicable provisions of the Bankruptcy Code and orders of the Court.

On November 19, 2009, in anticipation of filing the Chapter 11 Petitions, the Debtors entered into a Noteholder Restructuring Support Agreement with eight of ten of the beneficial holders (the Consenting Noteholders) of the Senior Notes, representing Consenting Noteholders holding approximately 88.1% of the outstanding principal amount of the Senior Notes. Pursuant to the Noteholder Restructuring Support Agreement, the Consenting Noteholders have agreed, subject to certain conditions, to support the Joint Chapter 11 Plan of Reorganization proposed by the Debtors, which was filed with the Chapter 11 Petitions.

On March 16, 2010, the Debtors entered into an Amended and Restated Plan Noteholder Restructuring Support Agreement (as amended, the Plan Support Agreement) with Consenting Noteholders holding approximately 88.1% of the outstanding principal amount of the Senior Notes. Pursuant to the Plan Support Agreement, the Consenting Noteholders

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have agreed to support a modified plan, in substantially the form of the Second Modified Joint Chapter 11 Plan of Reorganization for the Debtors as filed with the Court on March 16, 2010, and attached as Exhibit A to the Amended Plan Support Agreement (the "Second Modified Plan").

On April 9, 2010, the Debtors filed their Third Modified Joint Chapter 11 Plan of Reorganization (as modified, the "Plan") with the Court, which reflected further modifications to the Second Modified Plan. The terms of the Plan are hereafter described under the heading "The Third Modified Joint Chapter 11 Plan of Reorganization."

### *The Third Modified Joint Chapter 11 Plan of Reorganization*

Pursuant to the Plan, which is subject to Court approval, the holders of claims under the Senior Notes (the "Senior Note Claims") would, in exchange for the Senior Note Claims, receive their pro rata portion of (i) shares of new convertible preferred stock of GSIG (the "Preferred Shares"), which, on an as-converted basis, would represent approximately 53.8% of GSIG's post-consummation outstanding shares, (ii) new secured notes in the aggregate amount of \$110 million, (iii) excess cash available under the Plan to the extent certain allowed claims exceed \$22.5 million and (iv) a cash payment (the "Cash Payment") in an amount of \$69,315 for each day from and including the Petition Date until the plan distribution date. Under the terms of the Plan and because the Debtors commenced the Chapter 11 Cases by November 20, 2009, this Cash Payment would be reduced by \$2.1 million. On the effective date of the Plan, GSIG would also pay any and all interest accrued on the Senior Note Claims until the Petition Date. As of the Petition Date, there is approximately \$6.03 million in accrued and unpaid interest with respect to the Senior Notes. The Preferred Shares would have a 1x liquidation preference and be mandatorily redeemable after 8 years for cash or, if certain circumstances are met, common shares of GSIG. The Preferred Shares would be voted on an as-converted basis together with GSIG's common shares and share *pari passu* in any dividend declared on common shares, but not have any guaranteed fixed dividend rights. The interest rate on the new secured notes would be 12.25% and, at GSI US's option, subject to GSIG's compliance with a fixed charge coverage ratio defined in the indenture for the new secured notes to be entered into upon the effective date of the Plan, would be payable in kind at a compounded rate of 13%. The new secured notes would be issued by GSI US, guaranteed by GSIG, ten of GSI US's United States subsidiaries, and two of GSIG's Canadian subsidiaries and secured by substantially all the assets of GSI US and the guarantors.

As part of the Plan, GSIG's wholly owned subsidiary, GSI Group Limited, would, in exchange for claims under an unsecured note in the principal amount (as fixed pursuant to the Plan) of \$20 million, payable by GSI US to GSI Group Limited (the "GSI UK Note Claim"), receive (i) Preferred Shares, which, on an as-converted basis, would represent approximately 5.1% of GSIG's post-consummation outstanding shares, (ii) approximately \$10.5 million of the new secured notes, (iii) its pro rata share of the excess cash available under the Plan to the extent certain allowed claims exceed \$22.5 million and (iv) its pro rata share of the Cash Payment, as adjusted. On the effective date of the Plan, GSIG would also pay interest accrued on the GSI UK Note Claim until the Petition Date.

As contemplated by the Plan, existing shareholders would (i) retain 41.1% of GSIG's post-consummation outstanding shares, which would be issued in common shares and (ii) receive one series of three-year warrants to purchase a number of common shares equal to 10% of 111% of the post consummation outstanding shares of GSIG (that is, the number of shares of GSIG that would equal 10% of the shares of GSIG, including the Preferred Shares on an as-converted basis, before taking into account the number of shares represented by such warrants) at a strike price of \$2.50 per share.

Under the proposed Plan, all classes of claims, including all claims by vendors and suppliers, would be unimpaired and paid in full, except for the Senior Note Claims, the GSI UK Note Claim and the equity interest in GSIG.

The Plan provides that its effectiveness is subject to customary conditions, including, without limitation, that the effective date occurs on or before May 20, 2010, unless such date is extended pursuant to the Plan Support Agreement.

The Plan contemplates that the Debtors will continue to operate their businesses in substantially their current form. On November 23, 2009, the Debtors obtained the Court's approval of so-called first day motions providing for the continued payment of vendors and suppliers under normal terms in the ordinary course of business for goods and services provided to the Debtors prior to and after the Petition Date. On December 18, 2009, the Court approved the Plan Support Agreement. The Court further approved the Debtors' Disclosure Statement with respect to the Plan on January 8, 2010, and set a date for consideration of confirmation of the Plan for April 16, 2010.

The Plan provides that, following the effective date of the Plan, GSIG's Board of Directors would be comprised of seven directors, to include its Chief Executive Officer, three members to be appointed by the beneficial holders of the Senior Notes, two members to be appointed by the current shareholders of GSIG and one member to be appointed by the current board of



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directors of GSIG, which member will be selected from the members of GSIG's current board of directors as of the date of the Plan. The Plan anticipates that the current officers of GSIG would continue as officers of GSIG following the effective date of the Plan.

The recoveries summarized above and the other terms of the Company's restructuring are more fully described in the Plan.

### *The Plan Support Agreement*

The Debtors' proposed financial restructuring, as set forth in the Plan, has the support of Consenting Noteholders holding approximately 88.1% of the principal amount of the outstanding Senior Notes, representing 80% of all holders of the Senior Notes. The Plan Support Agreement was approved by the Court on December 18, 2009, and as noted above, was amended and restated on March 16, 2010.

The Plan Support Agreement requires the Consenting Noteholders, and their successors and assigns, (i) to timely file a notice with the Court indicating that the votes previously submitted by the Consenting Noteholders with respect to the Plan shall constitute and be deemed votes accepting and in favor of the Plan, (ii) not to object to confirmation of the Plan and not to object to, or otherwise commence, any proceeding to oppose or alter the Plan or support an alternative restructuring, (iii) not to withdraw, change or revoke their votes with respect to the Plan, except as otherwise permitted in the Plan Support Agreement, and (iv) except as otherwise permitted in the Plan Support Agreement, not to take any other action, including commencing any legal proceeding, that is inconsistent with, or that would materially prevent, hinder or delay the consummation of, the restructuring.

The support of the Consenting Noteholders under the Plan Support Agreement will terminate under certain circumstances, including, without limitation, if (i) the Debtors are in material breach of any obligations under the Plan Support Agreement, (ii) the Debtors file any motion or pleading with the Court that is inconsistent in a material respect with the Plan Support Agreement or the Plan, (iii) the Court grants relief that is materially inconsistent with the Plan Support Agreement or the Plan, (iv) the Debtors fail to achieve certain deadlines with respect to the approval of the Plan Support Agreement or the disclosure statement or confirmation or effectiveness of the Plan, (v) a trustee is appointed in the Chapter 11 Cases or any of the Chapter 11 Cases is dismissed or converted to a case under Chapter 7 of the Bankruptcy Code or if the Debtors make a motion for such appointment, dismissal or conversion, (vi) the Court enters an order invalidating, disallowing, subordinating, recharacterizing or limiting the principal and interest components of the Senior Note Claims or disgorging any amounts paid prior to the Petition Date from any holder of the Senior Note Claims or (vii) there is a Material Adverse Change to GSIG (as defined in the Plan Support Agreement).

The Plan Support Agreement provides that GSIG shall use its best efforts to (i) support and complete the restructuring and all transactions contemplated by the Plan, (ii) take any and all necessary and appropriate actions in furtherance of the restructuring, (iii) complete the restructuring and all transactions contemplated under the Plan within set time-frames, (iv) obtain any and all required regulatory and/or third-party approvals for the restructuring, and (v) not directly or indirectly seek, solicit, support, consent to, or participate in the negotiation or formulation of alternate plans of reorganization, certain other corporate transactions, such as mergers, dissolutions, or a sale of substantially all of GSIG's assets or any other action that is inconsistent with the reorganization as contemplated by the Plan Support Agreement.

### *Companies' Creditors Arrangement Act*

On April 8, 2010, the Debtors commenced certain parallel proceedings to the Chapter 11 Cases before the Court of Queen's Bench of New Brunswick (the "NB Court"), pursuant to section 46 of the Companies' Creditors Arrangement Act, for an order of the NB Court recognizing the foreign main proceeding constituting the Chapter 11 Cases and seeking relief from certain actions by the NB Court.

### *SEC Investigation*

As discussed in the Explanatory Note to the Annual Report on Form 10-K, we have conducted a Revenue Review of certain of our historic revenue transactions. On May 14, 2009, we received a notice from the SEC indicating that the SEC is conducting a formal investigation relating to our historical accounting practices and the restatement of our historical consolidated financial statements. The Company is cooperating fully with the SEC's investigation.

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### *Going Concern*

Operating in bankruptcy imposes significant risks and uncertainties on our business. See Item 1A Risk Factors Risks Relating to Bankruptcy for a discussion of the risks and uncertainties relating to our business and investing in our securities as a result of the Chapter 11 Cases.

The Company believes that when it emerges from bankruptcy it will be sufficiently capitalized. The Company expects that it will have assets that exceed its liabilities, and that those assets, as well as the net assets derived from its continuing operations, will be sufficient to meet the Company's obligations, including the obligations with respect to the payment of interest, and repayment of principal under the New Term Loan. Notwithstanding the Company's expectation upon its emergence from bankruptcy, uncertainties inherent in the bankruptcy process raise substantial doubt about the Company's ability to continue as a going concern. In particular, until the Plan is confirmed by the Court, the Company may be required to pay the Senior Note Claims under the original terms of the Senior Notes. The consolidated financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classification of liabilities that may result from the outcome of this uncertainty.

### **THE COMPANY'S CONTINUING OPERATIONS**

The Company operates in three segments, Precision Technology, Semiconductor Systems and Excel, which are described below.

#### *Precision Technology Segment*

The Company's Precision Technology Segment designs, manufactures, and markets lasers, optical scanners, optics, air bearing spindles, encoders, and thermal printers to customers worldwide. The Company's OEM products include those based on its core competencies in laser, precision motion and motion control technology. The Company sells the products in the Precision Technology Segment both directly and indirectly through resellers and distributors.

The Precision Technology Segment has six major product lines, including lasers, scanners, optics, printed circuit board spindles, encoders and thermal printers.

<b>Product Line</b>	<b>Key End Markets</b>	<b>Description</b>
<i>Lasers</i>	Industrial, Electronics, Automotive, Medical, Packaging and Aerospace	Applications include welding, cutting, drilling, surface marking, and deep engraving of metal and plastic parts.
<i>Scanners</i>	Industrial Electronics, Aerospace, and Medical Applications	High precision motors that, when coupled with a mirror, can direct a laser beam with a high degree of accuracy. Applications include laser marking and coding, laser machining and welding, high density via hole drilling of printed circuit boards, retinal scanning, laser-based vision correction, high resolution printing, 2D or 3D imaging, and laser projection and entertainment.
<i>Optics</i>	Aerospace, Telecommunications, And Industrial	Super flat and super polished optics, and high performance mirrors primarily used with a scanner to direct a laser light. Applications include all of the above (Scanners), and in addition, the deflection of laser beams in aircraft gyroscopes, and bending optical light beams that transmit telecommunications data.
<i>Printed Circuit Board Spindles</i>	Electronics	High-speed air bearing spindles used to drill very small and precise holes in printed circuit boards. Other applications include: semiconductors, industrial and printing.
<i>Encoders</i>	Electronics	Linear and rotary electro-optical tracking devices that measure movement with sub-micron accuracy. Applications include: motion control of semiconductor and electronic manufacturing equipment, confocal microscopes, positioning magnetic rings on hard drives, precision manufacturing and coordinate measuring systems.
<i>Thermal Printers</i>	Medical	Rugged paper tape printers for the medical instruments and defibrillator markets.

#### *Semiconductor Systems Segment*



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The Company's Semiconductor Systems Segment designs, develops and sells production systems that process semiconductor wafers using laser beams and high precision motion technology. The Company sells manufacturing systems to

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integrated device manufacturers and wafer processors. The Company's systems perform laser based processing on all of the following types of semiconductors: general wafers used for logic or memory purposes, dynamic random access memory (DRAM, NAND) chips and high performance analog chips.

Semiconductor manufacturers' main technology challenge is to meet the trend toward ever shrinking circuit sizes demanded by consumers of micro-electronics like cell phones. As semiconductor manufacturers put more memory on smaller die, the two critical challenges for production system suppliers are the ability to provide systems that can process wafers with manufacturing accuracy to the sub-micron level and to increase the wafer processing throughput.

The Semiconductor Systems Segment has three major product lines.

<b>Product Line</b>	<b>Key End Markets</b>	<b>Description</b>
<i>WaferRepair</i>	Semiconductor - DRAM and Flash Memory chips	Wafer Repair is used to raise production yields for 300mm and 200mm DRAM and NAND wafers to commercially acceptable levels.
<i>WaferTrim</i>	Semiconductor - high performance analog and mixed signal devices	Wafer Trim systems enable production of high performance integrated circuits by precisely trimming analog and mixed signal integrated circuits with a laser beam to achieve a specified electrical resistance.
<i>WaferMark</i>	Semiconductor - silicon suppliers and integrated circuit factories	WaferMark systems are used to mark silicon wafers with characters or markings at various stages of the wafer and integrated circuit manufacturing process. The marks are designed to aid process control and device traceability.

The Semiconductor Systems Segment also includes two smaller product lines, CircuitTrim and SVS CircuitTrim systems are used in the production of thick and thin film resistive components for surface mount technology electronic circuits, known as chip resistors, as well as thick and thin film hybrid circuits, and for adjusting the performance of complete multi-chip modules. SVS inspection equipment is used to inspect pre- and post- reflow solder paste and component placement on printed circuit boards.

*Excel Segment*

The Company's Excel Segment designs, manufactures and markets photonics-based solutions consisting of lasers, laser-based systems, precision motion devices and electro-optical components, primarily for industrial and scientific applications. The Company sells the products in the Excel Segment to customers worldwide, both directly and indirectly through resellers and distributors.

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The Excel Segment has four major product lines.

<b>Product Line</b>	<b>Key End Markets</b>	<b>Description</b>
<i>Lasers and Laser-Based Systems</i>	Industrial, Scientific and Homeland Security	Applications include cutting, marking, engraving and micro-machining, scientific research, remote sensing and automation.
<i>Scanners</i>	Industrial, Medical, Scientific, Military and Academic	High precision motors that, when coupled with a mirror, can direct a laser beam with a high degree of accuracy. Applications include product laser marking and coding, laser machining and welding, high density via hole drilling of printed circuit boards, scanning microscopy, retinal scanning and Optical Coherence Tomography imaging for laser-based biomedical diagnostics, laser-based vision correction, high resolution printing, holographic storage, semiconductor wafer inspection and processing, 2D or 3D imaging and laser projection and entertainment.
<i>Optics</i>	Scanning	Thin-filmed optics primarily used with a scanner to direct a laser light. Applications include optical scanners, laser systems, professional motion picture cameras and a myriad of other industrial and scientific applications, as well as interferometry and research and development.
<i>Light and Color Measurement</i>	Aerospace, Automotive, Lighting, Motion Picture, Research and Development and related industries	Color metrology systems are used by a wide variety of industries for research, quality control and on-line testing, including portable battery operated Spectro radio meter, photometers and video photometers.
<b>Products and Services</b>		

The Company's sales and gross margin contributions in 2008 were derived from the following business segments (dollars in thousands):

	<b>Sales</b>	<b>Gross Margin Percentage</b>
Precision Technology	\$ 146,616	33.5%
Semiconductor Systems	88,494	31.1%
Excel	55,612	37.2%
Intersegment sales eliminations(1)	(2,254)	(14.8)%
<b>Total</b>	<b>\$ 288,468</b>	<b>33.8%</b>

(1) Sales of the Precision Technology Segment's products to the Semiconductor Systems Segment.

**Customers**

The Company has a diverse group of customers that includes some of the largest global leaders in their industries. Many of the Company's customers participate in several market segments. In 2008, 2007 and 2006, no single customer accounted for 10% or more of sales.

Customers of our Semiconductor Systems Segment include some of the major semiconductor and silicon wafer producers. Most of these customers are end users who use our systems in their factories to manufacture products that include silicon wafers, memory chips, analog and hybrid micro-circuits in volume. A large number of them are based in Asia.

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Customers of our Precision Technology and Excel Segments include a large number of original equipment manufacturers who integrate our products into their systems for sale to end users. Some of our Precision Technology and Excel products are also sold directly to end users. Precision Technology Segment and Excel Segment customers include

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leaders in the semiconductor equipment, industrial systems, electronics, automotive, data storage, and medical equipment markets. A typical OEM customer will evaluate a Precision Technology Segment or Excel Segment product before deciding to incorporate it into a product or system. Customers generally choose suppliers based on a number of factors, including product performance, reliability, price, breadth of the supplier's product offering, and the geographical coverage offered by the supplier. Once Precision Technology Segment and Excel Segment products have been designed into a given OEM customer's product or system, there are generally significant barriers to subsequent supplier changes.

### ***Manufacturing***

The Company manufactures Precision Technology Segment products at facilities in Bedford, Massachusetts; Poole, Rugby and Taunton, United Kingdom and Suzhou, China. Semiconductor Systems Segment products are manufactured, assembled and tested in Bedford, Massachusetts. The Company manufactures Excel Segment products at facilities in Lexington, Massachusetts, East Setauket, New York; Orlando, Florida; Chatsworth, Oxnard and Santa Clara, California; Cambridge, Massachusetts; Mukilteo, Washington, and Ludwigsburg, Germany. Most of the Company's products are manufactured under ISO 9001 certification. Manufacturing functions are performed internally when management chooses to maintain control over critical portions of the production process or for cost related reasons. To the extent practical, the Company outsources the remaining portions of the production process. The Semiconductor Systems Segment focuses on outsourcing low value parts and modules and internally retains the tasks of final assembly of subsystems, testing and quality control.

All volume manufacturing of legacy laser products are moving from the Rugby, U.K. facilities, to other Company (including former Excel) laser manufacturing sites. The restructuring was significantly completed in 2009 and is projected to generate annual pretax savings in the range of \$2.0 to \$3.0 million.

### ***Research and Development and Engineering***

The Company continues to make a strong commitment to research and development for core technology programs directed at creating new products, product enhancements and new applications for existing products, as well as funding research into future market opportunities. Each of the markets the Company serves is generally characterized by rapid technological change and product innovation. The Company believes that continued timely development of new products and product enhancements to serve existing and new markets is necessary to remain competitive.

In 2008, 2007 and 2006 respectively, the Company incurred research and development and engineering expenses of \$33.4 million, \$29.9 million and \$30.1 million, which represents 11.6%, 10.3% and 11.6% of sales, respectively.

### ***Marketing, Sales and Distribution***

The Company sells its products worldwide through use of a direct sales force team and through distributors and sales agents. In the case of products sold through the Company's direct sales force, or local sales, applications and service teams work closely with our customers and leverage incremental supporting organizations from the Company to ensure customer satisfaction with our products. Our distributors work with customers in a similar fashion.

*Precision Technology* products are sold worldwide mostly through direct sales, as well as through distributors, primarily to OEMs. Precision Technology businesses have sales and service centers located in Massachusetts, Michigan, California, United Kingdom, Germany, Switzerland, Taiwan, China, Singapore and Japan. Sumitomo Heavy Industries Ltd. (a significant shareholder of the Company) is a key distributor for certain products in Japan. Because of the fundamental nature and relatively small physical size of the products, the Precision Technology Segment generally employs a factory direct strategy in support of its worldwide customer base except in its laser product line where parts and field technical support is significant.

*Semiconductor Systems* products are sold directly, or, in some territories, through distributors. End users include semiconductor integrated device manufacturers and electronic component and assembly firms. Sales activities are directed from the product business unit sites in North America, Europe, Japan and Asia Pacific. Field offices are located close to key customers' manufacturing sites to maximize sales and support effectiveness. Significant revenues are derived from the sales of parts, and the provisioning of services relating to the installed base of equipment previously sold to customers. The Company maintains field offices in Germany, Japan, South Korea, China, Taiwan and Singapore.

*Excel* products are sold worldwide mostly through direct sales, as well as through distributors, primarily to OEMs. Excel Segment businesses have sales and service centers located in Massachusetts, Florida, New York, Washington, California, United Kingdom, Germany, Italy, France, Malaysia, India and Japan. The Company also engages independent manufacturers' representatives for the sale of its Excel Segment products. Foreign sales of the Company's Excel Segment products are made primarily through foreign equipment distribution organizations. With the Company's acquisition of

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Excel, the Company also has a 50% equity ownership in a joint venture based in Mumbai, India. This joint venture markets, sells, installs and provides application support for certain of Excel's products in the southern Asian region.

### ***Competition***

The industries in which the Company participates are dynamic and highly competitive. The Company's markets in the photonics industry are characterized by intense competition and rapid technological change. Accordingly, the Company believes that it must continue to improve and refine its existing products and systems and develop new applications for its technology.

Competitive factors in the Company's Precision Technology and Excel Segments include: product performance, price, quality, features, flexibility, compatibility of products with existing systems, technical support, product breadth, market presence, on-time delivery and the Company's overall reputation. The main competitive factors in the Semiconductor Systems Segment include product performance, throughput and price. The Company believes that its products offer a number of competitive advantages, however, some of its competitors are substantially larger and have greater financial and other resources than the Company.

The table below illustrates the competition faced in the markets that the Company serves.

<b>Segment</b>	<b>Product Line</b>	<b>Main Competitor(s)</b>
<b>Precision Technology</b>	Lasers	Rofin-Sinar, Trumpf-Haas, IPG Photonics, Unitek-Miyachi, Lasag, and other specialized lasers and systems manufacturers
	Scanners	Fragmented among numerous suppliers, including Scanlabs GmbH
	Optics	Fragmented among numerous suppliers
	Printed circuit board spindles	ABL (owned by Hitachi), Mechatronics, Precise
	Encoders	Renishaw and Heidenhain
	Thermal printers	Advanced Printing Solutions
<b>Semiconductor Systems</b>	All semiconductor product lines	Electro Scientific Industries, Innolas, Shibaura, Omron
<b>Excel</b>	Lasers and laser-based systems	Rofin-Sinar, Coherent, Newport (Spectra-Physics), Electro, Foba, Laservall, SEI s.p.A., Cheval Frere, Fotona, E.O. Technics, Trump-Haas, IPG Photonics, Hans Laser, Electro Scientific Industries, ULS, Clark-MXR, Femtolaser, Thales Laser, Cyber Laser, New Wave Research, Quantel Lasers, Big Sky Lasers, Amplitude, Litron, Ekspla, and other specialized lasers and systems manufacturers
	Scanners	Fragmented among numerous suppliers
	Optics	Fragmented among numerous suppliers
	Light and color measurement	Minolta and Topcon

### ***Sources of Supply***

The Company depends on an uninterrupted supply of a large number of parts and components. Many of those parts and components are critical, and are available from a limited number of suppliers. The Company procures some components from a single source. The Company also relies on a limited number of independent contractors to manufacture subassemblies for some of its products. A disruption of this supply chain could potentially result in substantial manufacturing delays and additional costs. If suppliers or subcontractors experience difficulties that result in a reduction or interruption in supply to the Company, or fail to meet any of its manufacturing or quality requirements, the Company's business could be harmed unless or until it is able to secure alternative sources. These components and manufacturing services may not continue to be available to the Company at favorable prices, or at all.





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In the Precision Technology Segment, the Company sources most of the parts externally. However, the Company also manufactures many parts, including some critical parts, internally, particularly in the air bearing spindle business. The Company also purchases fully-functional electronics as well as certain key components, such as laser diodes, from external sources.

In the Semiconductor Systems Segment, the Company purchases major subsystems, such as lasers, motion stages, vision systems and software, fully-functional electronics and frames and racks, from the merchant market. Its optics components are both internally manufactured and externally purchased. In some cases, upper level assemblies and entire systems are outsourced to electronic manufacturing services companies.

In the Excel Segment, the Company relies upon unaffiliated suppliers for the material components and parts used to assemble its products. Most parts and components purchased from suppliers are available from multiple sources.

To date, the Company has not experienced any significant delays in obtaining parts and components for its products. The Company believes that it will be able to continue to obtain most required components and parts from a number of different suppliers, although there can be no assurance thereof. The Company cannot guarantee that its suppliers will continue to perform in a satisfactory fashion.

### ***Patents and Intellectual Property***

The Company relies upon a combination of copyrights, patents, trademarks, trade secret laws and restrictions on disclosure to protect our intellectual property rights. The Company holds approximately 400 issued patents, approximately 240 in the United States and approximately 160 in foreign countries. These patents are set to expire from 2010 through 2027. Additionally, the Company has approximately 230 pending patents, approximately 45 in the United States and approximately 185 in foreign countries. The issued patents cover various products in many of our key product categories, particularly semiconductor systems, optical scanning products, encoders, air bearing spindles, and lasers. In addition, we also have trademarks registered in the United States and foreign countries. We will continue to actively pursue application for new patents and trademarks as we deem appropriate. However, there can be no assurance that any other patents will be issued to the Company or that such patents, if and when issued, will provide any protection or benefit to the Company.

Although the Company believes that its patents and pending patent applications are important, the Company relies upon several additional factors that are essential to our business success, including: market position, technological innovation, know-how and product performance. There can be no assurance that the Company will realize any of these advantages.

We also protect our proprietary rights by controlling access to our proprietary information and by maintaining confidentiality agreements with our employees and consultants, and certain of our customers and suppliers. There can be no assurance, however, that other companies are not investigating or developing other technologies that are similar to ours. It is also possible that, despite our efforts, other parties may use, obtain or try to copy our technology and products, and that the steps we take to protect our propriety information may not provide meaningful protection in the event of misappropriation or disclosure. Further, policing authorized use of our intellectual property rights is difficult and time consuming and may involve initiating claims or litigation against third parties for infringement of our propriety rights, which could be costly. In particular, our efforts to protect our intellectual property rights may not be effective in some foreign countries where we operate or sell our products.

Additionally, we have received in the past, and could receive in the future, notices from third parties alleging that our products infringe patents or other proprietary rights. Although we believe that our products are non-infringing or that we have the patents and/or licenses to allow us to lawfully sell our products, we may be sued for infringement, which could adversely affect us. For a further discussion of the importance to our business of, and the risks attendant to, intellectual property rights, see **Risk Factors** in Item IA of this Annual Report on Form 10-K.

**Table of Contents****Human Resources**

Employees by functional area, as of December 31, 2009, are as follows:

	Number of Employees	Percentage
Production operations and field service	746	58%
Research and development	223	17
Selling, general and administrative	328	25
Total	1,297	100%

Employees by functional area, as of December 31, 2008, are as follows:

	Number of Employees	Percentage
Production operations and field service	919	59%
Research and development	252	16
Selling, general and administrative	397	25
Total	1,568	100%

**Geographic Information**

Information regarding the geographic components of the Company's sales and long-lived assets are provided in Note 15 of Notes to Consolidated Financial Statements included in this Annual Report on Form 10-K.

**Government Regulation**

The Company is subject to the laser radiation safety regulations of the Radiation Control for Health and Safety Act administered by the National Center for Devices and Radiological Health, a branch of the United States Food and Drug Administration. Among other things, these regulations require laser manufacturers to file new product and annual reports, to maintain quality control and sales records, to perform product testing, to distribute appropriate operating manuals, to incorporate design and operating features in lasers sold to end-users and to certify and label each laser sold to end-users as one of four classes (based on the level of radiation from the laser that is accessible to users). Various warning labels must be affixed and certain protective devices installed depending on the class of product. The National Center for Devices and Radiological Health is empowered to seek fines and other remedies for violations of the regulatory requirements. The Company believes that it is currently in compliance with these regulations.

The Company is subject to similar regulatory oversight, including comparable enforcement remedies, in the European markets it serves.

**Other**

Information concerning backlog and working capital may be found in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations.

**Available Information, Website and Access to Financial Filings**

The Company files annual, quarterly and current reports, proxy statements and other information with the SEC under the Securities Exchange Act of 1934 as amended (the Exchange Act). The Company's SEC filings are available on the Internet at the SEC's website at <http://www.sec.gov>. You may also access any document the Company has filed by visiting the SEC's public reference room in Washington, D.C. Please call the SEC at 1-800-SEC-0330 for further information about the public reference rooms.



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Financial and other information relating to the Company can also be accessed from the Company's Internet website at <http://www.gsig.com/investors/>. Except as otherwise stated in these documents, the information contained on our website or available by hyperlink from our website is not incorporated by reference into this report or any other documents we file with or furnish to the SEC.

The Company makes available, free of charge, copies of its annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act as soon as reasonably practicable after filing such material electronically or otherwise furnishing it to the SEC. In addition, the Company's reports and other information are filed with securities commissions or other similar authorities in Canada, and are available over the Internet at <http://www.sedar.com>.

Additionally, the Company posts a copy of its Code of Ethics on the Company website at <http://www.gsig.com/about/>.

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

The following information highlights some of the factors that could cause actual results to differ materially from the results expressed or implied by our forward-looking statements. Forward-looking statements should be considered in light of these factors. Factors that may result in such variances include, but are not limited to the following:

#### **Risks that Relate to our Review of Historic Revenue Transactions, Restatement of Historic Consolidated Financial Statements and Control Procedures**

*The matters relating to the review of our accounting practices and the recent restatement of our historical consolidated financial statements, including pending litigation, could have a material adverse effect on us.*

In connection with the closing of our financial statements for the quarter ended September 26, 2008, we discovered errors in the timing of revenue recognition of certain sales transactions in our Semiconductor Systems Segment. As a result of discovering these revenue recognition errors, we undertook a review of sales transactions in our Semiconductor Systems Segment and Precision Technology Segment for fiscal years 2006, 2007 and 2008. As a result of this review, we announced that the previously issued financial statements contained in the Company's Quarterly Reports on Form 10-Q for the periods ended March 28, 2008 and June 27, 2008 and Annual Reports on Form 10-K for the fiscal years ended December 31, 2007 and December 31, 2006 should no longer be relied upon. Additionally, we undertook a review of sales transactions in our Semiconductors Systems Segment and Precision Technology Segment during years 2004 and 2005, which we subsequently restated as reflected in this Annual Report. These efforts resulted in the delay of the filing of this Annual Report on Form 10-K, as well as our Quarterly Reports on Form 10-Q for the quarterly periods ended September 26, 2008, April 3, 2009, July 3, 2009 and October 2, 2009 and our Annual Report on Form 10-K for the year ended December 31, 2009 to correct the errors and prepare restated historical consolidated financial statements. The Revenue Review and the resulting restatements have required us to incur substantial expenses for legal, accounting, tax and other professional services and have diverted our management's attention from our business and could in the future adversely affect our business, financial condition, results of operations and cash flows.

The restatement of our prior financial statements has also exposed us to litigation. For example, in December 2008, a shareholder class action complaint was filed in the United States District Court for the District of Massachusetts against us, a former officer and a current officer and director. That complaint asserts claims under the federal securities laws, specifically Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, relating to the restatement of our financial results for 2006, 2007, and the first two quarters of 2008. The complaint alleges that we issued a series of false or misleading statements to the market concerning our revenues, earnings, and financial condition. The plaintiffs contend that such statements caused our stock price to be artificially inflated and seek unspecified damages. Additionally, on May 14, 2009, we received a notice from the SEC indicating that the SEC is conducting a formal investigation relating to our historical accounting practices and the restatement of our historical consolidated financial statements. We could also become subject to litigation brought on behalf of purchasers of our outstanding Senior Notes because of our restatement of the consolidated financial statements. The conduct and resolution of these and future related matters will be time consuming, expensive and distracting from the conduct of our business. Furthermore, if we are subject to adverse findings in any of these matters, we could be required to pay damages or penalties or have other remedies imposed upon us which could have a material adverse effect on our business, financial condition, results of operations and cash flows.

*The SEC has initiated a formal investigation relating to the review of our accounting practices and the restatement of our historical consolidated financial statements which could have a material adverse impact on us.*



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In addition to the litigation prompted by our restatement, we received a notice from the SEC indicating that the SEC is conducting a formal investigation relating to our historical accounting practices and the restatement of our historical consolidated financial statements. We are cooperating fully with the SEC investigation. The conduct and resolution of the SEC investigation and related matters could be time-consuming, expensive and distracting to the conduct of our business. In the event that the investigation results in an adversarial action or proceeding being brought against us, or any of our current or former officers or directors, our business (including our ability to complete financing transactions), and the trading price of our securities, may be adversely impacted. Additionally, if the SEC investigation continues for a prolonged period of time, it may have the same impact regardless of the ultimate outcome of the investigation. In the event of an adverse judgment in any action or proceeding, we may be required to pay damages or penalties, or other remedies may be imposed upon us, which could have a material adverse impact on our business, financial condition, results of operations and cash flows.

Additionally, while we believe we have made appropriate judgments in determining the correct reporting periods for restated revenues, the SEC may disagree with the manner in which we have accounted for and reported, or not reported, the financial impact. Accordingly, there is a risk we may have to further restate our historical financial statements, amend prior filings with the SEC, or take other actions not currently contemplated.

***Our Audit Committee, management and independent auditors have identified material weaknesses in our internal controls, and we may be unable to develop, implement and maintain appropriate controls in future periods.***

In connection with the review and restatement of our financial statements, our Audit Committee, management team and independent registered public accounting firm identified certain weaknesses in our internal controls that have been considered to be material weaknesses and significant deficiencies. Specifically, our material weaknesses include: inadequate and ineffective controls over the financial statement close process; inadequate and ineffective controls over the accounting for revenue recognition; inadequate and ineffective controls over the accounting for income taxes; and, inadequate and ineffective controls over the evaluation process for the impairment assessment for goodwill, intangible assets and other long-lived assets. Prior to the remediation of these material weaknesses, there remains risk that the transitional controls on which we currently rely will fail to be sufficiently effective, which could result in a material misstatement of our financial position or results of operations and require a restatement.

We are currently designing and implementing a new environment of procedures and controls intended to address the material weaknesses described above. While this design and implementation phase is underway, we are relying on extensive manual procedures, including the significant utilization of outside accounting professionals, to assist us with meeting the objectives otherwise fulfilled by an effective controls environment. We note that a system of procedures and controls, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the inherent limitations in all systems of procedures and controls, no evaluation can provide absolute assurance that all control issues including instances of fraud, if any, have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and breakdowns can occur because of simple error or mistake. Additionally, procedures and controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override. The design of any system of procedures and controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, our systems of procedures and controls, as we further develop and enhance them, may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective system of procedures and controls, misstatements due to error or fraud may occur and not be detected and could be material and require a restatement of our financial statements.

If we are unable to maintain appropriate internal controls, we may not have adequate, accurate or timely financial information, and we may be unable to meet our reporting obligations or comply with the requirements of the SEC or the Sarbanes-Oxley Act of 2002, which could result in the imposition of sanctions, including the inability of registered broker dealers to make a market in our common shares, or investigation by regulatory authorities. Any such action or other negative results caused by our inability to meet our reporting requirements or comply with legal and regulatory requirements or by disclosure of an accounting, reporting or control issue could adversely affect the trading price of our securities. Further and continued determinations that there are significant deficiencies or material weaknesses in the effectiveness of our internal controls could also reduce our ability to obtain financing or could increase the cost of any financing we obtain and require additional expenditures to comply with applicable requirements.

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**Risks Relating to Bankruptcy**

*We are subject to the risks and uncertainties associated with bankruptcy proceedings as a result of our filing for reorganization under Chapter 11 of the Bankruptcy Code on November 20, 2009.*

On November 20, 2009, we filed voluntary petitions with the Court to reorganize certain of our corporate entities under the Bankruptcy Code. This filing was made by our parent organization and two subsidiaries. We plan to continue to operate our business as a debtor-in-possession under the jurisdiction of the Bankruptcy Court and in accordance with the applicable provisions of the Bankruptcy Code. There can be no assurance that the Plan will be approved by the Bankruptcy Court or that any conditions precedent to its implementation will be satisfied or when, if ever, such confirmation and satisfaction will occur. Failure to obtain such confirmation or to satisfy such conditions to implementation may result in lengthier Chapter 11 proceedings as we attempt to negotiate and implement an alternative plan of reorganization.

For the duration of the Chapter 11 Cases, our operations will be subject to the risks and uncertainties associated with bankruptcy which include, among other things:

the relationships between us and our customers, employees, vendors, strategic partners and others may be negatively affected by the Chapter 11 Cases, including risks that our customers will be less likely to purchase our services, that our employees will seek out other opportunities or lack proper motivation to fulfill their commitments and that vendors and strategic partners could terminate their relationships with us or require financial assurances or enhanced performance to continue their business relationships with us, which may be unduly burdensome on our business and operations;

the actions and decisions of our creditors and other third parties with interests in our Chapter 11 Cases may be inconsistent with our plans;

objections to or limitations on our ability to obtain Court approval with respect to motions in the Chapter 11 Cases that we may seek from time to time or potential adverse decisions by the Court with respect to such motions;

our ability to obtain and maintain commercially reasonable terms with vendors, strategic partners and service providers;

our ability to obtain and maintain contracts that are critical to our operations;

our ability to retain customers; and

our ability to retain and motivate our management team and other key employees.

These risks and uncertainties could disrupt our business, adversely affect our relationships with customers, vendors, strategic partners or employees, or otherwise adversely affect our results of operations and financial condition. However, the ultimate impact of events that occur during these proceedings will have on our business, financial condition and results of operations, if any, cannot be accurately predicted or quantified. Our current Plan filed with the Court provides, among other things, that all existing equity in the Company will be heavily diluted. We can make no assurance that the price of our securities will not fluctuate or decrease substantially in the future. Accordingly, trading in our securities is highly speculative and poses substantial risks to purchasers of such securities, as holders may not be able to resell such securities or, in connection with our reorganization, may receive payment or other consideration that is less than the par value or the purchase price of such securities.

*Operating under the Bankruptcy Code may restrict our ability to pursue our business strategies.*

Under the Bankruptcy Code, we must obtain Court approval to, among other things:

sell assets outside the ordinary course of business;

consolidate, merge, sell or otherwise dispose of all or substantially all of our assets; and

engage in other activities that are outside the ordinary course of business.

***Our ability to continue as a going concern imposes significant risks to our operations.***

As set forth in the explanatory paragraph contained in the audit report on our 2008 Financial Statements of our independent registered public accounting firm, and due to the uncertainties inherent in the Chapter 11 process, there is substantial doubt as to our ability to continue as a going concern and our customers may become more reluctant to enter into arrangements with us.



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***We have a significant amount of debt which has been accelerated as a result of the Chapter 11 proceedings, which debt may not be restructured satisfactorily in the bankruptcy proceeding and could adversely affect our business, financial condition, results of operations and our ability to meet our payment obligations under our outstanding liabilities.***

We currently have \$210.0 million principal balance of debt related to our Senior Notes, the payment of which has been accelerated as a result of the Chapter 11 proceedings. Although the Company's obligation to repay the Senior Notes has been temporarily stayed as a result of the bankruptcy proceedings, and our proposed Plan, as submitted to the Bankruptcy Court, proposes, among other things, reducing the amount of our Senior Notes and certain other Company indebtedness, there can be no assurance that the Plan will be approved by the Bankruptcy Court or that our debt will be restructured satisfactorily. Even if the Plan is approved, we would still emerge from the Chapter 11 proceedings with substantial indebtedness that could adversely affect our business, financial condition and results of operations and our ability to meet our payment obligations under our outstanding liabilities. This level of debt could have significant consequences on our future operations, including:

Making it more difficult for us to meet our payment and other obligations under our outstanding debt;

Possibly resulting in an event of default if we fail to comply with the financial and other covenants contained in the indenture governing the restructured Senior Notes, which event of default could result in all amounts thereunder becoming immediately due and payable;

Reducing the availability of our cash flow to fund working capital, capital expenditures, acquisitions and other general corporate purposes, and limiting our ability to obtain additional financing for these purposes;

Limiting our flexibility in planning for, or reacting to, and increasing our vulnerability to, changes in our business, the industry in which we operate and the general economy; and

Placing us at a competitive disadvantage compared to our competitors that have less debt or are less leveraged.

Any of the above-listed factors could have an adverse effect on our business, financial condition and results of operations and our ability to meet our payment obligations under our outstanding liabilities.

***The pursuit of the Chapter 11 has consumed and will continue to consume a substantial portion of the time and attention of our management.***

The requirements of the Chapter 11 Cases has consumed, and will continue to consume, a substantial portion of our management's time and attention and leave them with less time to devote to the operations of our business. This diversion of management's attention may have a material adverse effect on the conduct of our business, and, as a result, on our financial condition and results of operations, particularly if the Chapter 11 Cases are protracted.

***We may experience increased levels of employee attrition due to the Chapter 11 Cases.***

Because of the Chapter 11 Cases, our employees are facing considerable distractions and uncertainty. In addition, due to the global economic environment, we have conducted reductions of our workforce during 2008 and 2009. A loss of key personnel or a substantial reduction in our workforce or material erosion of employee morale could have a material adverse effect on our business, particularly if the Chapter 11 Cases are protracted. Our ability to motivate and retain key employees is restricted by provisions of the Bankruptcy Code, which limit or prevent our ability to implement a retention program or take other measures intended to motivate key employees to remain with us throughout the pendency of the Chapter 11 Cases without Court approval. The loss of the services of any members of our senior management could impair our ability to execute our strategy and, as a result, could have a material adverse effect on our results of operations and financial condition.

***We could be subject to claims made after the date that we filed for bankruptcy and other claims that are not discharged in the Chapter 11 Cases, which could have a material adverse effect on our results of operations and financial condition.***



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We are currently subject to claims in various legal proceedings and may become subject to other legal proceedings in the future. Although we will seek to satisfy and discharge all claims made against us prior to the date of the bankruptcy filing (which claims are generally stayed during the Chapter 11 Cases), we may not be successful in doing so. Any claims arising after the date of our bankruptcy filing, and possible certain other claims that arose prior to the filing, may not be subject to discharge in the Chapter 11 Cases. The outcome of each of these claims, including our ability to have such claims satisfied and discharged in the Chapter 11 Cases, cannot, at this time, be determined, nor can the liability that may potentially result from a negative outcome be reasonably estimated presently for every case. The liability that we may ultimately incur with respect to any of these claims (in the event of a negative outcome) may be in excess of amounts that have currently been accrued with respect to such claims and, as a result, may have a material adverse effect on our results of operations and financial condition.

**Risks Relating to Noncompliance with NASDAQ and SEC Requirements**

*NASDAQ has made a delisting determination with respect to our common shares, we are not presently in compliance with all applicable continued listing requirements or standards of the NASDAQ Global Select Market, and we are not listed on any other national securities exchange. It will likely be more difficult for stockholders and investors to sell our common shares or to obtain accurate quotations of the share price of our common shares.*

As a result of our failure to timely file certain of our periodic reports with the SEC, on November 3, 2009, we received a delisting determination from NASDAQ and were also notified that trading in our common shares would be suspended effective on November 5, 2009. Although we timely appealed the Panel's determination to the Listing Council, on January 15, 2010, the Listing Council notified the Company that it affirmed the Panel's decision to delist the Company's securities. On March 15, 2010, the Company received notification from the NASDAQ Board that it has declined to call for review the January 15, 2010 decision of the Listing Council. Accordingly, pursuant to Listing Rule 5825, the Listing Council's decision represents the final decision of NASDAQ. In accordance with Listing Rule 5830 and Rule 12d2-2 under the Securities Exchange Act of 1934, NASDAQ filed an application on Form 25 with the SEC on April 5, 2010, to delist the Company's securities from NASDAQ. The application will become effective ten days after filing.

In addition to our failure to timely file required periodic reports, we are not in compliance with certain other continued listing requirements of NASDAQ. For example, the NASDAQ rules require that, among other things, we maintain a minimum bid price of at least \$1 per share. On September 16, 2009, we were notified by NASDAQ that the closing bid price per share of our common shares had been below \$1 per share for thirty consecutive business days and, in accordance with applicable NASDAQ rules, we were given an exception until March 15, 2010 to regain compliance with the minimum bid price standard. The NASDAQ rules also require that we hold an annual shareholders meeting within twelve months of our fiscal year end. In connection with our previously mentioned appeal to the Listing Council, we notified NASDAQ that we were unable to hold an annual shareholders meeting in fiscal year 2009, as required, although we recently announced that a meeting date of April 30, 2010 has been set for the Company's next annual shareholders meeting. In addition, the NASDAQ rules provide that NASDAQ has discretion to suspend or terminate the listing of a company that files for protection under the Bankruptcy Code. Each of the foregoing may have contributed to the Listing Council's decision to affirm the Panel's decision to delist our common shares. As a result of the NASDAQ delisting determination, the Company's common shares are currently quoted on the Pink OTC Markets Inc., continuing under the trading symbol GSIGQ. Stocks trading on the over-the-counter market are typically less liquid than stocks that trade on a national securities exchange. Trading on the over-the-counter market may also negatively impact the trading price of our common shares. In addition, the liquidity of our common shares may be impaired, not only in the number of shares that are bought and sold, but also through delays in the timing of transactions, and coverage by security analysts and the news media, if any, of our Company. Stockholders may find it difficult to resell their shares of our common shares, due to the delisting proceedings and the likely effect of the Chapter 11 Cases on our common shares. The delisting of our common shares from NASDAQ may also result in other negative implications, including the potential loss of confidence by customers, strategic partners and employees, and loss of institutional investor interest in our common shares.

*We recently discovered that we have inadvertently failed to file with the SEC a registration statement relating to securities issued under our 2006 Plan. As a result, we may have engaged in multiple issuances of duly authorized but unregistered securities and we may be subject to civil litigation, enforcement proceedings, fines, sanctions and/or penalties.*

It has come to our attention that between March 2007 and March 2010, we inadvertently issued unregistered shares to fifty-two employees and directors under our 2006 Plan in an amount of approximately 773,037 common shares with a total fair market value at the date of issuance of approximately \$3.9 million. These securities were also issued without an appropriate restrictive legend.

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Although we believed that we and our counsel at the time had filed the appropriate registration statement on Form S-8, it came to our attention during the preparation of this Annual Report on Form 10-K that a registration statement on Form S-8 or other appropriate form had not been filed and the issuances were not made pursuant to a valid exemption from the applicable federal and state securities laws. Accordingly, it may be determined that such issuances were not exempt from registration or qualification under federal and state securities laws, and we did not obtain the required registrations or qualifications. As a result, we may be subject to civil litigation, enforcement proceedings, fines, sanctions and/or penalties.

We may also be subject to claims by participants in the 2006 Plan for rescission of their acquisitions of common shares under the 2006 Plan under federal securities laws until the expiration of the applicable statute of limitations period, which is one year under federal law from the date of transaction. If applicable, such participants may have the right to rescind their purchases for an amount equal to the purchase price for the shares (or if the shares have been disposed of, claims for any damages with respect to any loss on such disposition) plus interest from the date of purchase. However, under applicable provisions of federal law (including section 510(b) of the Bankruptcy Code (11 U.S.C. § 510(b)), and in connection with our Chapter 11 Cases, if the proposed Plan is confirmed, the holders of any such damage claims and related rescission or other rights would, we believe, be entitled to receive a distribution under the Plan of common shares of the reorganized Company only. We believe that the most likely result is that any such claims, if allowed, would result in the holder receiving that quantity of common shares in the reorganized Company that are determined by a court to result in equal treatment of such claim holders and existing equity holders. Furthermore, rescission or damages claims of a shareholder who holds the above described unregistered shares, but receives new shares, as contemplated by the Plan, would be discharged upon the Company's emergence from the bankruptcy proceedings. Such new shares would be issued pursuant to an exemption from registration under §1145 of the Bankruptcy Code and be freely tradable by holders who are not deemed to be underwriters.

### ***We may be unable to timely file certain periodic reports with the SEC.***

We did not timely file with the SEC this Annual Report or our Quarterly Report on Form 10-Q for the quarter ended September 26, 2008; our Annual Report on Form 10-K for the year ended December 31, 2009; nor our Quarterly Reports on Form 10-Q for each of the quarters ended April 3, 2009, July 3, 2009 and October 2, 2009. We may continue to be unable to timely file our annual and quarterly periodic reports with the SEC in the future. Following the commencement of the Chapter 11 Cases, our management has been particularly strained by the considerable attention required for administering the Chapter 11 Cases. In addition, due to the continuing demands on management's time and attention in connection with the Chapter 11 Cases, as well as any attrition that we may experience in the future, we cannot make any assurances as to whether or when we will be able to complete and file our periodic reports in the future.

Also as a result of our delayed filings with the SEC, we will be ineligible to register our securities on Form S-3 for sale by us or resale by others until one year from the date the last delinquent filing is made. We may use Form S-1 to raise capital or complete acquisitions, but doing so could increase transaction costs and adversely impact our ability to raise capital or complete acquisitions of other companies in a timely manner.

### **Risks that are Derived from our Operations**

***The results of our operations could be adversely affected by economic and political conditions and the effects of these conditions on our customers' businesses and level of business activity.***

A large portion of our sales are dependent on the need for increased capacity or replacement of inefficient manufacturing processes, because of the capital-intensive nature of our customers' businesses. These sales also tend to lag behind in an economic recovery longer than other businesses. There was a rapid softening of the economy and tightening of the financial markets in the second half of 2008 that continued into the first half of 2009. This slowing of the economy has reduced the financial capacity of our customers and possibly our potential customers, thereby slowing spending on the products and services we provide. If the current down turn lasts longer than expected, and if a recovery does not begin or if a new general economic slowdown commences, we may not be able to meet anticipated revenue levels on a quarterly or annual basis. A severe and/or prolonged economic downturn or a negative or uncertain political climate could adversely affect our customers' financial condition and the timing or levels of business activity of our customers and the industries we serve. This may reduce the demand for our products or depress pricing for our products and have a material adverse effect on our results of operations. Changes in global economic conditions could also shift demand to products or services for which we do not have competitive advantages, and this could negatively affect the amount of business that we are able to obtain. In addition, if we are unable to successfully anticipate changing economic and political conditions, we may be unable to effectively plan for and respond to those changes, and our business could be negatively affected.

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***Our business depends significantly upon capital expenditures which are subject to cyclical market fluctuations.***

The semiconductor and electronics materials processing industries are cyclical and have historically experienced periods of oversupply, resulting in downturns in demand for capital equipment, including the products that we manufacture. The timing, length and severity of these cycles, and their impact on our business, are difficult to predict. Further, our order levels or results of operations for a given period may not be indicative of order levels or results of operations for subsequent periods. We cannot assure investors that demand for our products will increase or that demand will not decrease. For the foreseeable future, our operations will continue to depend upon industries that are subject to market cycles, which, in turn, could adversely affect the market for our products.

***Cyclical variations may have the most pronounced effect on our Semiconductor Systems Segment, which concentrates in the semiconductor and electronics industries.***

There is no assurance that we will not be impacted from continuation of the current economic slowdown or face future slowdowns as we have experienced in previous cyclical fluctuations or that the impact will be more or less significant compared to historical fluctuations.

***Our business success depends upon our ability to respond to fluctuations in product demand.***

If business declines, we may be required to reduce costs while at the same time maintaining the ability to motivate and retain key employees. We must also continually invest in research and development which may inhibit our ability to reduce costs in a down cycle. Additionally, long product lead-times create a risk that we may purchase or manufacture inventories of products that we are unable to sell. While we practice inventory management, we can offer no assurances that our efforts to mitigate this risk will be successful.

***During a period of increasing demand and rapid growth, we must be able to increase manufacturing capacity quickly.***

Our inability to quickly increase production in response to a surge in demand could prompt customers to look for alternative sources of supply or leave our customers without a supply, both of which events could harm our reputation and make it difficult for us to retain our existing customers or to obtain new customers.

***The success of our business requires that we continually innovate.***

Technology requirements in our markets are consistently advancing. We must continually introduce new products that meet evolving customer needs. Our ability to grow depends on the successful development, introduction and market acceptance of new or enhanced products that address our customer's requirements. Developing new technology is a complex and uncertain process requiring us to accurately anticipate technological and market trends and meet those trends with responsive products. Additionally, this requires that we manage the transition from older products to minimize disruption in customer ordering patterns, avoid excess inventory and ensure adequate supplies of new products. Failed market acceptance of new products or problems associated with new product transitions could harm our business.

***Delays in delivery of new products could have a negative impact on our business.***

Our research and development efforts may not lead to the successful introduction of products within the time period our customers demand. Our competitors may introduce new or improved products, processes or technologies that make our current or proposed products obsolete or less competitive. We may encounter delays or problems in connection with our research and development efforts. Product development delays may result from numerous factors, including:

changing product specifications and customer requirements;

the inability to manufacture products cost effectively;

difficulties in reallocating engineering resources and overcoming resource limitations;

changing market or competitive product requirements; and

unanticipated engineering complexities.

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New products often take longer to develop, have fewer features than originally considered desirable and achieve higher cost targets than initially estimated. There may be delays in starting volume production of new products and/or new products may not be commercially successful.

*Our quarterly results of operations may fluctuate in the future. As a result, we may fail to meet or exceed the expectations of securities analysts or investors, which could cause our stock price to decline.*

We sell a relatively small number of high revenue semiconductor systems within any period. These systems are complex and may have multiple elements for customer delivery including overall systems, spare parts, extended warranties, installation and training and may be subject to customer acceptance criteria. In certain transactions, we recognize all or a portion of revenue upon shipment provided title and risk of loss has passed to the customer, evidence of an arrangement exists, fees are contractually fixed or determinable, collectability is reasonably assured through historical collection results and regular credit evaluations, and there are no uncertainties regarding the receipt or timing of customer acceptance. As a result, it is often difficult to project the timing of product revenue recognition. Consequently, our revenue and financial results could vary significantly from expectations in a particular quarter if anticipated orders from even a few customers are not received and fulfilled in time to satisfy customer obligations to the extent necessary to permit revenue to be recognized under generally accepted accounting principles. In addition, our product order backlog at the beginning of each quarter may not include all systems needed to achieve expected revenues for that quarter. Because we may build systems according to forecast, the absence of a significant backlog for an extended period of time could adversely affect financial results.

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### ***Customer order timing and other factors beyond our control may lead to an inability to meet our financial forecasts.***

Changes in customer order timing and the existence of certain other factors beyond our control may lead to our inability to meet financial forecasts. Such factors include:

fluctuations in our customers' businesses;

timing and recognition of revenues from customer orders;

timing and market acceptance of new products or enhancements introduced by us or our competitors;

availability of parts from our suppliers and the manufacturing capacity of our subcontractors;

timing and level of expenditures for sales, marketing and product development;

changes in the prices of our products or of our competitors' products; and

fluctuations in exchange rates for foreign currency.

A large percentage of our sales come from products with high selling prices and significant lead times. We may receive several large orders in one quarter from a customer and then receive no orders from that customer in the next quarter. As a result, the timing and recognition of sales from customer orders can cause significant fluctuations in our operating results from quarter to quarter.

A delay in a shipment or failure to meet our revenue recognition criteria near the end of a reporting period due, for example, to rescheduling or cancellations by customers or to unexpected difficulties experienced by us, may cause sales in the period to fall significantly below expectations and may have materially adverse effects on our operations for that period. Our inability to adjust quickly enough could magnify the adverse effects of that revenue shortfall on our results of operations.

As a result of these factors, our results of operations for any quarter are not necessarily indicative of results to be expected in future periods. We believe that fluctuations in quarterly results may cause the market prices of our common shares to fluctuate, perhaps substantially.

### ***Our director and officer liability insurance may not cover the Company's exposure in the securities class action litigation.***

During the last several months, the parties have been in settlement discussions and the parties have reached an agreement in principle to settle the securities class action lawsuit. The agreement in principle contemplates that the Company's insurance carrier will contribute to the settlement. The total settlement amount is well within the Company's insurance policy limits; the Company's contribution to the settlement amount would be minimal and reflects the balance of the company's self-insured retention. The agreement in principle is subject to a number of contingencies including confirmatory discovery by the Lead Plaintiff, after which Lead Plaintiff may affirm or void the agreement in principle, preliminary and final approval by the District Court, and to the extent required by law, approval by the Bankruptcy Court. If the agreement in principle is not finalized, there are no assurances that any future settlement or judgment will either be covered by the Company's liability insurance policies or fall within their limits.

### ***Our effective tax rates are subject to fluctuation, which could impact our financial position, and our estimates of tax liabilities may be subject to audit, which could result in additional tax assessments.***



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Our effective tax rates are subject to fluctuation as the income tax rates for each year are a function of taxable income levels in numerous tax jurisdictions, our ability to utilize recorded deferred tax assets, taxes or penalties resulting from tax audits and credits and deductions as a percentage of total taxable income. Further, tax law changes may cause our effective tax rates to fluctuate between periods.

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***We maintain significant cash balances, and in the past we have maintained and may in the future maintain foreign exchange contracts, where significant changes in interest rates, credit ratings or foreign currency rates could result in materially adverse effects to income.***

These balances create financial exposure to changing interest and currency rates. We have attempted to mitigate these risks by, in the past and possibly in the future, purchasing foreign exchange contracts, and by investing in United States government issued treasury bills. However, if long term interest rates or foreign currency rates were to change rapidly, we could incur material losses. Further, if management chooses to invest in less risk adverse investment vehicles, the risk of losing principal and/or interest could increase.

***Our investments in auction rate securities are subject to risks which may cause losses and affect the liquidity of these investments.***

As of December 31, 2008, we held auction rate securities, recorded at a fair value of \$25.1 million, and with a par value of \$32.3 million. These securities were acquired as part of our purchase of Excel in 2008. Auctions for some of these auction rate securities have failed, and there is no assurance that auctions on the remaining auction rate securities in our investment portfolio will succeed in the future. An auction failure means that the parties wishing to sell their securities could not do so. As a result, our ability to liquidate and fully recover the carrying value of our auction rate securities in the near term may be limited or not exist. The uncertainties in the credit markets have prevented us and other investors from liquidating holdings of auction rate securities at times when we, or other investors, would have chosen to do so.

We have had some success in liquidating these holdings during 2009. Of the \$32.3 million in par value securities that we held as of December 31, 2008, we sold \$19.3 million of the securities, and recorded net realized gains on our sales of these securities. As of December 31, 2009, we continue to hold remaining securities with a par value of \$13.0 million. If the credit ratings of the issuer, the bond insurers or the collateral deteriorate further, or if the issuers of these auction rate securities are unable to successfully close future auctions, we may further reduce the carrying value of these investments and may in the future be required to record impairment charges against these investments, some of which may be considered other-than-temporary impairment charges. We may be required to wait until market stability is restored for these instruments or until the final maturity of the underlying notes (up to 30 years) to recover our investment.

***International operations are an expanding part of our business and our operations in foreign countries subject us to risks not faced by companies operating exclusively in the United States.***

During the year ended December 31, 2008, 69.3% of our revenue was derived from operations outside of the United States. The scope of our international operations subjects us to risks which could materially impact our results of operations including:

foreign exchange rate fluctuations;

social unrest in countries where we operate;

climatic or other natural disasters in regions where we operate;

increases in shipping costs or increases in fuel costs;

longer payment cycles;

acts of terrorism;

greater difficulty in collecting accounts receivable;

use of incompatible systems and equipment;

problems staffing and managing foreign operations in diverse cultures;

protective tariffs;

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trade barriers and export/import controls;

transportation delays and interruptions;

reduced protection for intellectual property rights in some countries; and

the impact of recessionary foreign economies.

We cannot predict whether the United States or any other country will impose new quotas, tariffs, taxes or other trade barriers upon the importation of our products or supplies or gauge the effect that new barriers would have on our financial position or results of operations.

***There are inherent risks as we increase our focus on overseas operations.***

We manufacture certain products in plants in the United Kingdom and China. Manufacturing in overseas locations creates risks, including the possibility that as operations are transferred or expanded in foreign locations we may not be able to produce products to the quality standards or deliver products on time as our customers have come to expect. This possibility may come about due to an inability to find qualified personnel overseas. It is also possible that after an overseas transition, we may find that we have been producing products with latent defects that come to light only after a long period of operation. Transitioning a business to an overseas location has many additional risks such as developing solid financial, enterprise resource planning (ERP) and customer relationship management (CRM) systems.

***Economic, political or trade problems with foreign countries could negatively impact our business.***

We are increasingly outsourcing the manufacture of sub assemblies to suppliers based in China and elsewhere overseas. Economic, political or trade problems with foreign countries could substantially impact our ability to obtain critical parts needed in the timely manufacture of our products.

***Customs rules are complex and vary within legal jurisdictions in which we operate. Failure to comply with local customs regulations could be discovered during a foreign government customs audit that may produce a substantial penalty.***

Customs rules are complex and vary within legal jurisdictions in which we operate and there can be no assurance that there will be no control failure around customs enforcement despite the precautions we take. A failure with local customs regulations could be discovered during a foreign government customs audit and could result in a substantial penalty and a material impact on our financial results. We seek to mitigate this risk by maintaining export control systems and an internal customs staff charged with the responsibility of strictly complying with all applicable import/export laws. Further, we attempt to maintain arms length transactions with our foreign subsidiaries and their customers.

***We have a history of operating losses and we may not be able to sustain or grow the current level of profitability.***

We incurred operating losses on an annual basis from 1998 through 2003 and again in 2008. No assurances can be given that we will sustain or increase the level of profitability in the future based on extrinsic market forces, and the market price of our common shares may decline as a result.

***Our Ability to Utilize Our Net Operating Loss Carryforwards and Other Tax Attributes will be Limited as a Result of Our Plan of Reorganization and is Dependent on Our Ability to Generate Sufficient Future Taxable Income.***

We have significant net operating loss carryforwards ( NOLs ) and other tax attributes. Section 382 of the Internal Revenue Code of 1986, as amended, limits a corporation's ability to utilize NOLs and other tax attributes following a Section 382 ownership change. We expect that we will undergo a Section 382 ownership change upon the implementation of our Plan of Reorganization and, consequently, our ability to utilize our NOLs and other tax attributes will be limited. In order to prevent an ownership change during our Chapter 11 proceedings, the Bankruptcy Court has entered an order that places certain restrictions on trading in our common shares. However, despite the order, we can provide no assurances that an ownership change has not or will not occur prior to emergence. Such a change prior to emergence could further limit our ability to utilize our NOL carryforwards. A significant limitation in our ability to utilize our NOL carryforwards could have a negative impact on our financial results.



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In addition, our ability to use future tax deductions is dependant on our ability to generate sufficient future taxable income in the U.S. In determining our provision for income taxes, our tax attributes and liabilities and any valuation allowance recorded against our net tax attributes require subjective judgment and analysis. We consistently evaluate our tax attributes based on tax recoverable in the carryback period, existing deferred tax liabilities, tax planning strategies and future taxable income. Although we anticipate using certain of our tax attributes to generate tax refunds from prior years, our ability to recover all our tax attributes in certain jurisdictions depends upon our ability to continue to generate future profits. If actual results differ from our plans or we do not achieve the desired level of profitability in a given jurisdiction, we may be required to increase the valuation allowance on our tax attributes by taking a charge to the statement of operations, which could have a material negative result on our financial results.

***Our reliance upon third party distribution channels subjects us to credit, inventory, business concentration and business failure risks beyond our control.***

We sell products through resellers, distributors, original equipment manufacturers ( OEMs ) and system integrators. We sell certain lasers through a 50% owned Indian joint venture. The holder of the other 50% of the joint venture is not a related party. Selling products through third parties can subject us to credit and business risks. Our sales also depend upon the ability of our OEM customers to develop and sell systems that incorporate our products. Adverse economic conditions, large inventory positions, limited marketing resources and other factors influencing these OEM customers could have a substantial impact upon our financial results. We can not assure investors that our OEM customers will not experience financial or other difficulties that could adversely affect their operations and, in turn, our financial condition or results of operations.

***We are exposed to the credit risk of some of our customers and to credit exposures in weakened markets, which could result in material losses.***

Customers with liquidity issues may lead to additional bad debt expense. We monitor individual customer payment capability in granting open credit arrangements, and seek to limit such open credit to amounts we believe our customers can pay, and we maintain reserves we believe are adequate to cover exposure for doubtful accounts. However, there can be no assurance that our open credit customers will pay the amounts they owe to us or that the reserves we maintain will be adequate to cover such credit exposure. Our customers' failure to pay and/or our failure to maintain sufficient reserves could have a material adverse effect on our operating results and financial condition.

In addition, to the extent that the ongoing turmoil in the credit markets makes it more difficult for some customers to obtain financing, those customers' ability to pay may be adversely impacted, which in turn could have a material adverse effect on our business, operating results and financial condition.

While we generally sell a portion of our sales directly to customers future sales may be derived through distributors. As distributors tend to have more limited financial resources than original equipment manufacturers ( OEM ) and end-user customers, they generally represent sources of increased credit risk. Additionally, in the event that the ongoing turmoil in the credit markets makes it more difficult for some customers to obtain financing, those customers' ability to pay could be adversely impacted, which in turn could have a material adverse impact on our business, operating results and financial condition.

***We are exposed to the risks that others may violate our intellectual property rights.***

Our future success depends in part upon our intellectual property rights, including trade secrets, know-how and continuing technological innovation. There can be no assurance that the steps we take to protect our intellectual property rights will be adequate to prevent misappropriation, or that others will not develop competitive technologies or products outside of our patented property. There can be no assurance that other companies are not investigating or developing other technologies that are similar to ours, that any patents will issue from any application filed by us or that, if patents do issue, the claims allowed will be sufficiently broad to deter or prohibit others from marketing similar products. In addition, there can be no assurance that any patents issued to us will not be challenged, invalidated or circumvented in a legal or administrative proceeding, or that our patents and know how will provide a competitive advantage to us.

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***Our intellectual property rights may not be protected in foreign countries.***

Our efforts to protect our intellectual property rights may not be effective in some foreign countries where we operate or sell. Many U.S. companies have encountered substantial problems in protecting their property rights against infringement in foreign countries. If we fail to adequately protect our intellectual property in these countries, it could be easier for our competitors to sell competing products in foreign countries.

***Our success depends upon our ability to protect our intellectual property and to successfully defend against claims of infringement by third parties.***

We have received in the past, and could receive in the future, notices from third parties alleging that our products infringe patent or other proprietary rights. We believe that our products are non-infringing or that we have the patents and/or licenses to allow us to lawfully sell our products throughout the world. However, we may be sued for infringement. In the event any third party makes a valid claim against us or our customers for which a license was not available to us on commercially reasonable terms, we would be adversely affected. Adverse consequences may also apply to our failure to avoid litigation for infringement or misappropriation of proprietary rights of third parties.

***We operate in highly competitive industries, and if we lose competitive advantages, our business would suffer adverse consequences.***

Some of our competition comes from established competitors, some of which have greater financial, engineering, manufacturing and marketing resources than we do. Our competitors will continue to improve the design and performance of their products and introduce new products. It is possible that we may not successfully differentiate our current and proposed products from the products of our competitors, or that the marketplace will not consider our products to be superior to competing products. To remain competitive, we will be required to invest heavily in research and development, marketing and customer service and support. It is also possible that we may not be able to make the technological advances necessary to maintain our competitive position, or our products will not receive market acceptance. We may not be able to compete successfully in the future, and increased competition may result in price reductions, reduced profit margins, loss of market share and an inability to generate cash flows that are sufficient to maintain or expand our development of new products.

***Our business strategy includes finding and making strategic acquisitions and divestitures. There can be no assurance that we will be able to continue to make acquisitions or divestitures that provide business benefit.***

We acquired an optics business in the United Kingdom in 2007, we completed our acquisition of Excel in August 2008 and we sold our U.S. Optics Business in October 2008. We expect to continue to evaluate potential acquisitions and divestitures as part of our long-term strategic plan. Our identification of suitable acquisition candidates involves risks inherent in assessing the values, strengths, weaknesses, risks, synergy and profitability of acquisition candidates, including the effects of the possible acquisition on our business, diversion of management's attention from our core businesses and risks associated with unanticipated problems or liabilities. We cannot assure investors our efforts will be sufficient, or that acquisition candidates will be receptive to our advances or that any acquisition we may make would be accretive to earnings. We also cannot assure investors that we will find suitable purchasers in the event that we identify a potential divestiture candidate in the future. Further, given our significant debt and inability to use Form S-3, we may have difficulty obtaining financing for such strategic acquisitions.

***We may fail to successfully complete the integration of Excel into our business and, as a result, may fail to realize the synergies, cost savings and other benefits expected from the acquisition. Further, Excel's performance has not been in accordance with our expectations, which has had, and could continue to have a material adverse effect on our financial condition.***

We may fail to successfully complete the integration of Excel into our business and, as a result, may fail to realize the synergies, cost savings and other benefits expected from the acquisition. The revenue we expected from Excel did not materialize in 2008, which contributed significantly to the impairment charge we recorded in 2008. We may continue to fail to grow and build revenues and profits in Excel's business lines or achieve sufficient cost savings through the integration of customers or administrative and other operational activities. Furthermore, we must achieve these objectives without adversely affecting our revenues. If we are not able to successfully achieve these objectives, the anticipated benefits of the acquisition may not be realized fully or at all, or it may take longer to realize them than expected, and our results of operations could be materially adversely affected.

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Further, our ability to maintain and increase profitability of Excel's business lines will depend on our ability to manage and control operating expenses and to generate and sustain increased levels of revenue. Our expectations to achieve more consistent and predictable levels of revenue and to increase Excel's profitability may not be realized, and such revenues and profitability may decline as we integrate Excel's operations into our business. If Excel's revenues grow more slowly than we anticipate, or if its operating expenses are higher than we expect, we may not be able to sustain or increase its profitability, in which case our financial condition will suffer and our stock price could decline. For example, as discussed in Note 6 of Notes to Consolidated Financial Statements, in 2008, we experienced decreased performance relative to our expectations for our acquisition of Excel. The decreased performance contributed to our having recorded a significant impairment charge against the value of assets that were initially attributed to the goodwill, intangible assets and other long-lived assets of Excel. Should there be continued deterioration in Excel's performance, future impairment changes may be required to be recorded.

*We continue our leadership transition, which could have a material effect on our business.*

We continuously review our management, business and organizational structures. There are risks associated with changes in strategy and management at the executive and/or director level, and changes in product or operational focus. During 2008, and in early 2009, we experienced significant turnover in our management team, including our Chief Financial Officer, our General Counsel and certain senior members of our various segments or operating groups. There can be no assurance that any of the anticipated or other prospective management changes will not have a negative material effect on the Company.

*Our operations could be negatively affected if we lose key executives or employees or are unable to attract and retain skilled executives and employees as needed.*

Our business and future operating results depend in part upon our ability to attract and retain qualified management, technical, sales and support personnel for our operations on a worldwide basis. The loss of key personnel could negatively impact our operations. Competition for qualified personnel is intense and we cannot guarantee that we will be able to continue to attract, train and retain qualified personnel.

*The Company conducted an internal review of potential issues related to the Foreign Corrupt Practices Act and voluntarily shared information relating to that review with the SEC in the third quarter of 2009. These matters could have a material adverse effect on us. Further, our reputation and our ability to do business may be impaired by improper conduct by any of our employees, agents or business partners.*

During the Revenue Review, the Audit Committee and its advisors identified certain potential issues related to the Foreign Corrupt Practices Act (FCPA), in particular in China, and referred those issues to the Company for review. With the assistance of outside legal counsel, the Company conducted and completed an internal review of those potential issues and voluntarily shared information relating to the internal review with the SEC in the third quarter of 2009. While we have not received any further requests from the SEC on this internal FCPA review, we cannot predict whether the SEC will request any further information from the Company regarding the internal FCPA review or whether the SEC will take any other action.

Additionally, we cannot provide assurance that our internal controls will always protect us from reckless or criminal acts committed by our employees, agents or business partners that would violate US and/or non-US laws, including the laws governing payments to government officials, competition, money laundering and data privacy. Any such improper actions could subject us to civil or criminal investigations in the US and in other jurisdictions, and could lead to substantial civil or criminal, monetary and non monetary penalties against us or our subsidiaries. Following the aforementioned internal review, we updated our FCPA compliance policies and enhanced our FCPA training program.

*We have undertaken restructuring activities, and we will continue to assess our operating structure.*

Our ability to reduce operating expenses is dependent upon the nature of the actions we take to reduce expense and subsequent ability to implement those actions and realize expected cost savings. For example, in the past years we shifted certain of our operations in the United States and United Kingdom to China to reduce expenses. We have undertaken actions to consolidate redundant or excess personnel that have arisen due to our acquisition of Excel in August 2008, and due to the contracting demand for certain of our products due to the global economic slowdown. We have also divested of other businesses. There can be no assurance that these actions will provide us economic benefit. Further, there is a risk that these actions may ultimately prove detrimental to operations and sales, or to our intellectual property protections.



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### ***We expect to be consolidating some of our operations for greater efficiency.***

There is execution risk in these plans. We can not assure investors that economies of scale will or can be realized as a result of any historic or planned restructuring activities. These actions will take time and will include substantial operational risks, including the possible disruption of manufacturing lines. We can not assure investors that any moves would not disrupt business operations or have a material impact on results.

In addition, any decision to limit investment in, dispose of or otherwise exit business activities may result in the recording of special charges, such as technology write-offs, workforce reduction costs, charges relating to consolidation of excess facilities, or a loss on the sale of assets. Our estimates with respect to the useful life or ultimate recoverability of our carrying basis of assets, including intangible assets, could change as a result of such decisions. Further, our estimates related to the liabilities for excess facilities are affected by changes in real estate market conditions. Our December 2008 assessment of the carrying value of goodwill and intangible assets resulted in substantial write downs. Additionally, we are required to perform goodwill impairment tests on an annual basis and during the year in certain circumstances. There can be no assurance that future goodwill and intangible assets impairment tests will not result in a change to earnings.

### ***Product defects or problems with integrating our products with other vendors products may seriously harm our business and reputation.***

Complex products that we produce can contain latent errors or performance problems. There have been instances where we have found errors immediately after launch of new products, and there have been instances where we have also found latent errors in our products. We cannot always resolve errors that we believe would be considered serious by our customers before implementation, thus our products are not error-free. These errors or performance problems could be detrimental to our business and reputation. In addition, customers frequently integrate our products with other vendors products. When problems occur in a combined environment, it may be difficult to identify the source of the problem. These problems may cause us to incur significant warranty and repair costs, divert the attention of our engineering personnel from our product development efforts and cause significant customer relations problems. These problems may also complicate our determination of the timing and amount of revenue recognition. To date, defects in our products or those of other vendors products with which our products are used by our customers have not had a material negative effect on our business relationships with our customers. However, we cannot be certain that a material negative impact will not occur in the future.

### ***We depend on limited source suppliers that could cause substantial manufacturing delays if supply disruption occurs.***

Many of our products are manufactured with components that are designed by an outside supplier. While we attempt to mitigate risks associated with our reliance on single suppliers by actively managing our supply chain, we still source some components from single vendors. We also rely on a limited number of independent contractors to manufacture subassemblies for some of our products, particularly in our Semiconductor Systems. There can be no assurance that our current or alternative sources will be able to continue to meet all of our demands on a timely basis. If suppliers or subcontractors experience difficulties, or fail to meet any of our manufacturing requirements, our business would be harmed until we are able to secure alternative sources, if any, on commercially reasonable terms.

### ***We also depend on suppliers that provide high precision parts.***

Any such parts that have latent or known defects, may materially impact relations with our customers if they cause us to miss our scheduled shipment deadlines. If latent defects are incorporated into our products and discovered later, there could be a material impact on our revenues. We seek to reduce the risk of defects by selecting and qualifying alternative suppliers for key parts, and by monitoring the quality of products coming from key suppliers.

### ***Production difficulties and product delivery delays could materially adversely affect our business.***

We assemble our products at our facilities in the United States, the United Kingdom and China. If use of any of our manufacturing facilities were interrupted by a natural disaster or otherwise, our operations could be negatively impacted until we could establish alternative production and service operations. In addition, we may experience production difficulties and product delivery delays in the future as a result of:

mistakes made while transferring manufacturing processes between locations;

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changing process technologies;

ramping production;

installing new equipment at our manufacturing facilities; and

shortage of key components.

***Increased governmental regulation of our business could materially adversely affect us.***

We are subject to many governmental regulations, including but not limited to the laser radiation safety regulations of the Radiation Control for Health and Safety Act administered by the National Center for Devices and Radiological Health, a branch of the United States Food and Drug Administration, and certain health regulations related to the manufacture of products using beryllium, an element used in some of our structures and mirrors. Among other things, these regulations require us to file annual reports, to maintain quality control and sales records, to perform product testing, to distribute appropriate operating manuals, to incorporate design and operating features in products sold to end-users and to certify and label our products. Various warning labels must be affixed and certain protective devices installed depending on the class of product. We are subject to regulatory oversight, including comparable enforcement remedies, in the markets we serve.

***Changes in governmental regulations may reduce demand for our products or increase our expenses.***

We compete in many markets in which we and our customers must comply with federal, state, local and international regulations, such as environmental, health and safety and food and drug regulations. We develop, configure and market our products to meet customer needs created by those regulations. Any significant change in regulations could reduce demand for our products, which in turn could materially adversely affect our business, operating results and financial condition.

***We may require additional capital to support business growth, and this capital may not be available on acceptable terms or at all.***

We may require additional funds to respond to business challenges, including the need to develop new products or enhance our existing products, enhance our operating infrastructure and acquire complementary businesses and technologies. Accordingly, we may need to engage in equity or debt financings to secure additional funds. If we raise additional funds through further issuances of equity or convertible debt securities, our existing stockholders could suffer significant dilution, and any new equity securities we issue could have rights, preferences and privileges superior to those of holders of our common shares. Further, our existing Senior Notes may restrict or impede our ability to obtain additional debt financing. Any debt financing secured by us in the future could include restrictive covenants relating to our capital raising activities and other financial and operational matters, which may make it more difficult for us to obtain additional capital and to pursue business opportunities, including potential acquisitions. In addition, we may not be able to obtain additional financing on terms favorable to us or at all. If we are unable to obtain adequate financing or financing on terms satisfactory to us when we require it, our ability to continue to support our business growth and to respond to business challenges could be significantly limited. In addition, the terms of any additional equity or debt issuances may adversely affect the value and price of our common shares.

Due to the prevailing global economic conditions that largely began in 2008, many businesses do not have access to the capital markets on acceptable terms. In addition, as a result of this global credit market crisis, conditions for acquisition activities have become very difficult as tight global credit conditions have adversely affected the ability of potential buyers to finance acquisitions. Although these conditions have not immediately affected our current plans, these adverse conditions are not likely to improve significantly in the near future and could have a negative impact on our ability to execute on future strategic activities.

**Risks that Relate to Our Common Shares**

***Trading in our securities during the pendency of the Chapter 11 Cases is highly speculative and poses substantial risks. If our pre-arranged Plan of reorganization that we filed is confirmed by the Court, our common shares will be heavily diluted. If our Plan of reorganization is not confirmed by the Court, we may be unable to come to terms with the holders of our Senior Notes, and holders of such common shares likely will not receive any distribution with respect to, or be able to recover any portion of, such investment.***



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If our Plan of reorganization is confirmed by the Court, our common shares will be heavily diluted. If our Plan of reorganization is not confirmed by the Court, an alternative plan of reorganization could be approved by the Court, resulting in more or less dilution compared with the Company's proposed Plan or as a result of which our common shares could be cancelled upon the approval of the Court and if that were to occur the holders thereof would not be entitled to receive, and would not receive or retain, any property or interest in property on account of such common shares. Trading prices are very volatile and frequently bear no relationship to the expected recovery by the holders of such securities in Chapter 11 reorganization proceedings. Accordingly, we urge that extreme caution be exercised with respect to existing and future investments in our equity securities and any of our other securities.

***Holders of our common shares are subject to the risk of additional and substantial dilution to their interests as a result of future issuances of common shares.***

In the future, we may issue additional equity securities to raise capital or restructure our existing debt and our stock option holders may exercise all or some of the options that are outstanding or may be outstanding. These additional issuances would dilute existing share ownership.

***Future sales of a substantial number of our common shares in the public market could adversely affect the trading price of our shares and impair our ability to raise funds in future stock offerings.***

Future sales of a substantial number of our common shares in the public market or the perception that such sales could occur, could adversely affect the prevailing market price of our common shares and could make it more difficult for us to raise additional capital through the sale of equity securities.

***The market price of our common shares has been and may continue to be subject to wide fluctuations, and this may make it difficult for you to resell the common shares when you choose to or at prices you find attractive.***

Our stock price historically has been, and may continue to be, volatile. Various factors contribute to the volatility of the stock price, including:

the current general economic downturn and any future general economic downturns that impacts the purchasing decisions of our significant customers or the timing and size of their orders;

fluctuation in demand for our products and the timing and size of customer orders;

the cancellation or deferral of existing customer orders or the renegotiation of existing contractual commitments;

the length and variability of the sales cycle for our products;

changes in our pricing policies, the pricing policies of our competitors and the prices of the components of our products;

our ability to develop, introduce and ship new products and product enhancements that meet customer requirements in a timely manner;

the mix of product configurations sold;

our ability to attain and maintain production volumes and quality levels for our products;

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costs related to acquisitions of complementary products, technologies or businesses;

corporate restructurings, including layoffs;

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the timing of revenue recognition and the application of complex revenue recognition accounting rules to our customer arrangements;

announcements of quarterly operating results and revenue and earnings forecasts by us, our competitors or our customers;

failure to achieve financial forecasts, either because expected sales do not occur or because they occur at lower prices or on terms that are less favorable to us;

rumors, announcements or press articles regarding changes in our management, organization, operations or prior financial statements;

changes in revenue and earnings estimates by securities analysts;

announcements of planned acquisitions by us or by our competitors;

announcements of new or planned products and enhancements by us, our competitors or our customers;

gain or loss of a significant customer;

our involvement in legal proceedings and the entry of judgments or decisions adverse to us;

inquiries and/or proceedings by the SEC, NASDAQ, law enforcement or other regulatory bodies; and

acts of terrorism and the threat of war.

While we cannot predict the individual effect that these factors may have on the market price of our common shares, these factors, either individually or in the aggregate, could result in significant volatility in our stock price during any given period of time. Additionally, the stock market has recently experienced extreme price volatility, which has adversely affected and may continue to adversely affect the market price of our common shares for reasons unrelated to our business or operating results.

***Our directors, executive officers and each of our greater than 5% stockholders and their affiliates have substantial control over the outstanding shares of our common shares, which could limit your ability to influence the outcome of key transactions, including a change of control.***

Our directors, executive officers and each of our greater than 5% stockholders and their affiliates, in the aggregate, together beneficially own a substantial amount of the outstanding shares of our common shares. As a result, these stockholders, if acting together, may be able to influence or control matters requiring approval by our stockholders, including the election of directors and the approval of mergers, acquisitions or other extraordinary transactions. They may have interests that differ from yours and may vote in a way with which you disagree and which may be adverse to your interests. This concentration of ownership may have the effect of delaying, preventing or deterring a change of control of our company, could deprive our stockholders of an opportunity to receive a premium for their common shares as part of a sale of our company and might affect the market price of our common shares.

***Certain provisions of our articles of incorporation may delay or prevent a change in control of our company.***

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Our corporate documents and our existence as a corporation under the laws of New Brunswick subject us to provisions of Canadian law that may enable our Board of Directors to resist a change in control of our company. These provisions include:

limitations on persons authorized to call a special meeting of stockholders;

advance notice procedures required for stockholders to nominate candidates for election as directors or to bring matters before an annual meeting of stockholders; and

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a shareholder rights plan.

These anti-takeover defenses could discourage, delay or prevent a transaction involving a change in control of our company. The transactions contemplated by our Plan in the Chapter 11 Cases will not trigger our existing shareholder rights plan. These provisions could also discourage proxy contests and make it more difficult for stockholders to elect directors of their choosing and cause us to take other corporate actions that stockholders desire.

**Item 1B. Unresolved Staff Comments**

Not applicable.



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The principal owned and leased properties of the Company and its subsidiaries are listed in the table below.

Location	Principal Use	Current Segment (a)	Approximate Square Feet	Owned/Leased
<b>Facilities</b>				
Bedford, Massachusetts, USA	Manufacturing, R&D, Marketing, Sales and Administrative	1,2,4	147,000	Leased; expires in 2013.
Rugby, United Kingdom (b)	Manufacturing, R&D, Marketing, Sales and Administrative	1	113,000	Owned and partially leased to third parties.
Poole, United Kingdom (c)	Manufacturing, R&D, Marketing, Sales and Administrative	1	88,000	2 units owned; 2 units with land leases through 2073 and 2078 (two sites)
Orlando, Florida, USA	Manufacturing, R&D, Marketing, Sales and Administrative	3	80,000	Owned
East Setauket, New York, USA	Manufacturing, R&D, Marketing, Sales and Administrative	3	65,000	Owned
Mukilteo, Washington, USA	Manufacturing, R&D, Marketing, Sales and Administrative	3	63,000	Owned
Suzhou, People's Republic of China	Manufacturing, R&D, Marketing, Sales and Administrative	1	55,000	Leased; expires in 2011
Santa Clara, California, USA	Manufacturing, Marketing, Sales and Administrative	3	44,388	Leased; expires in 2010
Lexington, Massachusetts, USA	Manufacturing, Marketing, Sales and Administrative	3	33,339	Leased; expires in 2016
Ludwigsburg, Germany	Manufacturing, R&D, Marketing, Sales and Administrative	3	22,500	Leased; expires in 2011
Chatsworth, California, USA	Manufacturing, R&D, Marketing, Sales and Administrative	3	22,000	Owned
Taunton, United Kingdom	Manufacturing, R&D, Marketing and Sales	1	19,000	Leased; expires in 2017
Mumbai, India	Service, R&D, Sales and Administrative	3	16,769	Owned
Oxnard, California, USA	Manufacturing and Administrative	3	14,000	Leased; expires in 2014

(a) The facilities house product lines that belong to the following segments:

- 1 Precision Technology Segment
- 2 Semiconductor Systems Segment
- 3 Excel Segment
- 4 Corporate

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- (b) At December 31, 2008, the Rugby, U.K. building is classified as an asset available for sale. This property was sold in October 2009 for approximately \$3.6 million. Prior to the property being sold, approximately 14% of the space had been leased to third parties.
- (c) At December 31, 2008, one of the two Poole, U.K. buildings was classified as an asset available for sale. This property constitutes 37,000 square feet of space. This property was sold in February 2009, for approximately \$0.5 million.

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Additional research and development, sales, service and logistics sites are located in California, Colorado, United Kingdom, Germany, France, Italy, Japan, Korea, Taiwan, China, Malaysia and Sri Lanka. These additional offices are in leased facilities occupying approximately 83,000 square feet in the aggregate.

A portion of the Company's leased facility in Bedford, Massachusetts, and its owned facility in Orlando, Florida are currently underutilized. The Company leases a 29,000 square foot building in Munich, Germany. However, as a result of prior year restructuring activities, this building had more space than the Company needed in this location and in 2007 this building was fully sublet through the end of the lease in 2013. The Company also leases 13,000 square feet of space in Novi, Michigan. However, as a result of a 2008 restructuring activity, this space was abandoned, and is also being sublet. The Company continues to pay for this space in Novi until the expiration of the lease in 2012.

As of December 31, 2009 and 2008, we were productively utilizing substantially all of the space in our facilities, except for space identified above as underutilized, unoccupied, or as subleased to third parties.

**Item 3. Legal Proceedings**

The Company's French subsidiary, GSI Lumonics SARL (Lumonics), is subject to a claim by a customer, SCGI, that a Laserdyne 890 system delivered in 1999 had unresolved technical problems. During the third quarter of 2005, GSI France, parent of Lumonics, filed for bankruptcy protection, which was granted by the French court on July 7, 2005. On April 18, 2006, the court fixed SCGI's claim against Lumonics at 598,079 Euros, plus court costs and expert fees of 85,945 Euros. SCGI accepted the court's determination. SCGI is now demanding that the Liquidator bring an action in the United Kingdom against GSI Group Ltd., the parent corporation of GSI France. The Company is not aware of any facts to support a claim. The Company's French counsel is addressing these points directly with the Liquidator. At this time, the Company does not believe it will be required to make any payments regarding this action. Accordingly, nothing has been accrued in the Company's accompanying consolidated financial statements.

On August 6, 2008, a purported stockholder of Excel Technology, Inc., a subsidiary of the Company, filed a complaint seeking certification of a class action lawsuit in the Supreme Court of the State of New York, County of New York, docketed as Joseph Choquette, v. Antoine Dominic, Steven Georgiev, Donald E. Weeden, Ira J. Lamel, J. Donald Hill and Excel Technology, Inc., Index No. 08/602294 (the Choquette Action) against Excel and each of its directors. The Choquette Action purports to be brought individually and on behalf of all public stockholders of Excel. The Choquette Action alleges that Excel's director defendants breached their fiduciary duties to Excel's stockholders in connection with the proposed tender offer by the Company and that each of the defendants aided and abetted such alleged breach of Excel's director defendants' fiduciary duties. Based on these allegations, the Choquette Action seeks, among other relief, an order declaring the action to be a class action, enjoining preliminarily and permanently the tender offer and the merger with the Company, rescinding, to the extent already implemented, the tender offer and the merger with the Company or any of the terms thereof or awarding rescissory damages, directing that the defendants account to plaintiff and other members of the class for all damages caused by them and account for all profits and any special benefits obtained as a result of a breach of their fiduciary duties to the purported stockholder and other members of the class, awarding plaintiff the costs of the Choquette Action including a reasonable allowance for the expenses of plaintiff's attorneys and experts and granting plaintiff and other members of the class such further relief as the court deems just and proper. On August 14, 2008, Excel and the individual defendants in the Choquette Action filed a motion to dismiss the lawsuit. On August 18, 2008, the plaintiff in the Choquette Action filed a motion seeking a preliminary injunction to enjoin consummation of the tender offer and to require Excel to issue additional and supplementary disclosures in Excel's Schedule 14D-9 filing. On August 19, 2008, the court denied plaintiff's motion for a preliminary injunction. On April 15, 2009, the court granted defendants' motion to dismiss and entered judgment dismissing the complaint with prejudice.

On December 12, 2008, in connection with the delayed filing of its results for the quarter ended September 26, 2008, and the announcement of a review of revenue transactions, a putative shareholder class action alleging federal securities violations was filed in the United States District Court for the District of Massachusetts against us, a former officer and a current officer and director. Specifically, the complaint alleges that the Company and the individual defendants violated Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, and seeks recovery of damages in an unspecified amount. The action was brought on behalf of a putative class of shareholders who purchased the Company's stock between April 30, 2008 and December 3, 2008. A lead plaintiff, Mason Tenders District Council Trust Funds, was appointed on May 8, 2009. On July 1, 2009, the Court ordered lead plaintiff to file a consolidated or amended complaint within 30 days of the Company's filing of restatements for certain of its historical financial results with the SEC. During the last several months, the parties have been in settlement discussions and the parties have reached an agreement in principle to settle this lawsuit. The settlement would, in general, cover purchasers of the common stock of the Company between February 27, 2007 and June 30, 2009. The agreement in principle is subject to a number of contingencies including confirmatory discovery by the Lead Plaintiff, after which Lead Plaintiff may affirm or void the agreement in principle, preliminary and final approval by the District Court, and to the extent required by law, approval by the Bankruptcy Court. Although the agreement in principle is not final, the total settlement amount is well within the Company's insurance policy limits; the Company's contribution to the settlement amount would be limited to the balance of the company's self-insured retention.



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The Company is also subject to various legal proceedings and claims that arise in the ordinary course of business. The Company does not believe that the outcome of these claims will have a material adverse effect upon the Company's financial conditions or results of operations but there can be no assurance that any such claims, or any similar claims, would not have a material adverse effect upon the Company's financial condition or results of operations.

### ***Chapter 11 Cases***

On November 20, 2009, the Debtors filed voluntary petitions for relief under Chapter 11 of the Bankruptcy Code in the United States Bankruptcy Court for Delaware, as discussed in Item 1 Business. Under the Bankruptcy Code, the filing of a petition automatically stays most actions against the Company, including most actions to collect pre-petition indebtedness or to exercise control over the property of our bankruptcy estates. Absent further order of the Bankruptcy Court, no party, subject to certain exceptions, may take any action, also subject to certain exceptions, to recover on pre-petition claims against the Debtors. We expect substantially all of our pre-petition liabilities will be resolved under our plan of reorganization if not otherwise satisfied pursuant to orders of the Bankruptcy Court.

### ***SEC Investigation***

As discussed in the Explanatory Note to the Annual Report on Form 10-K, we have conducted a Revenue Review of certain of our historic revenue transactions. On May 14, 2009, we received a notice from the SEC indicating that the SEC is conducting a formal investigation relating to our historical accounting practices and the restatement of our historical consolidated financial statements. The Company is cooperating fully with the SEC's investigation.

### **Item 4. Submission of Matters to a Vote of Security Holders**

None.

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***Market Information***

The Company's common shares are currently quoted on the Pink OTC Markets Inc., continuing under the trading symbol GSIGQ. In 2008 and 2007 the Company's common shares, no par value, traded on The NASDAQ Stock Market under the symbol GSIG. The following table sets forth the high and low sales prices during the periods indicated.

	2008		2007	
	High	Low	High	Low
First Quarter	\$ 9.63	\$ 7.49	\$ 9.96	\$ 8.26
Second Quarter	8.49	7.30	10.80	9.59
Third Quarter	7.95	3.29	11.30	9.34
Fourth Quarter	3.86	0.43	11.57	9.10

***Holder***

As of the close of business on December 31, 2009, there were approximately 101 holders of record of its common shares. Since many of the common shares are registered in nominee or street names, the Company estimates that the total number of beneficial owners is considerably higher.

***Dividend Policy***

The Company has never declared or paid cash dividends on its common shares. The Company currently intends to retain any current and future earnings to finance the growth and development of its business and, therefore, does not anticipate paying any cash dividends in the foreseeable future.

***Recent Sales of Unregistered Securities******1. 2006 Plan***

The Company recently discovered that it inadvertently failed to file with the SEC a registration statement on Form S-8 relating to securities issued under its 2006 Plan. As a result, the Company inadvertently issued unregistered shares of common stock as described in further detail below. Since becoming aware of this issue, the Company has been unable to take corrective steps to register such securities since the Company has not been current in its SEC periodic reporting obligations and is therefore not eligible to rely on a registration statement on Form S-8 or any other registration statement until it becomes current in its periodic reporting requirements under the Securities Exchange Act of 1934, as amended. The Company has instituted a moratorium on the granting of all equity awards and share issuances until a registration statement on Form S-8 is on file.

The Company's 2006 Plan was approved by the Company's shareholders in May 2006 and issuances of equity awards thereunder were available to substantially all of its employees, consultants and directors worldwide. From March 2007 through March 2010, the Company issued approximately 773,037 duly authorized common shares with a total fair market value at the date of issuance of approximately \$3,889,796 to fifty-two employees and directors under its 2006 Plan. However, the Company's management subsequently determined that these common shares issued pursuant to the 2006 Plan were inadvertently not registered under the Securities Act of 1933 or applicable state securities law requirements prior to issuance and were issued without an appropriate restrictive legend. As a result, the Company may be subject to civil litigation, enforcement proceedings, fines, sanctions and/or penalties.

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The Company may also be subject to claims by participants in the 2006 Plan for rescission of their acquisitions of common shares under the 2006 Plan under federal securities laws until the expiration of the applicable statute of limitations period, which is one year under federal law from the date of transaction. If applicable, such participants may have the right to rescind their purchases for an amount equal to the purchase price for the shares (or if the shares have been disposed of, claims for any damages with respect

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to any loss on such disposition) plus interest from the date of purchase. However, under applicable provisions of federal law (including section 510(b) of the Bankruptcy Code (11 U.S.C. § 510(b)), and in connection with our Chapter 11 Cases, if the Company's proposed Plan is confirmed, the holders of any such damage claims and related rescission or other rights would, the Company believes, be entitled to receive a distribution under the Plan of common shares of the reorganized Company only. The Company believes that the most likely result is that any such claims, if allowed, would result in the holder receiving that quantity of common shares in the reorganized Company that are determined by a court to result in equal treatment of such claim holders and existing equity holders. Furthermore, rescission or damages claims of a shareholder who holds the above described unregistered shares, but receives new shares, as contemplated by the Plan, would be discharged upon the Company's emergence from the bankruptcy proceedings. Such new shares would be issued pursuant to an exemption from registration under §1145 of the Bankruptcy Code and be freely tradable by holders who are not deemed to be underwriters.

As noted above, the Company's failure to (i) register the common shares underlying the 2006 Plan and (ii) issue the common shares pursuant to a valid exemption from such registration requirements was inadvertent and the Company has always treated the common shares issued under the 2006 Plan as outstanding for financial reporting purposes. Consequently, these unregistered transactions do not represent any additional dilution.

*2. Excel Technology, Inc.*

In August 2008, in connection with our acquisition of Excel, the Company entered into a Warrant Agreement with certain holders of our Senior Notes, dated August 20, 2008 (the "Warrant Agreement"), pursuant to which the Company issued and sold to such noteholders warrants to purchase common shares of the Company (the "Warrants"). The Warrants were issued in a private transaction in reliance upon the exemption from registration contained in Section 4(2) of the Securities Act of 1933, as amended. The Warrants were subsequently net exercised in exchange for 5,858,495 common shares and such common shares were simultaneously registered pursuant to a Registration Statement on Form S-3 filed with the SEC in October 2008.



**Table of Contents*****Purchases of Equity Securities by the Issuer and Affiliated Purchaser***

The following table provides information about purchases by the Company during the year ended December 31, 2008 of equity securities that were registered by the Company pursuant to Section 12 of the Exchange Act:

<b>Period</b>	<b>Total Number of Shares Purchased</b>	<b>Average Price Paid per Share</b>	<b>Total Number of Shares Purchased as Part of Publicly Announced Plan or Programs</b>	<b>Maximum Number (or Approximate Dollar Value) of Shares that May Yet be Purchased Under Plans or Programs</b>
January 2 - January 17, 2008	248,700	\$ 8.67	248,700	\$ 1,227,837
March 7 - March 20, 2008	116,000	\$ 8.26	116,000	\$ 25,269,803
March 31 - May 2, 2008	293,000	\$ 8.15	293,000	\$ 22,886,157
May 5 - May 19, 2008	114,767	\$ 8.19	114,767	\$ 21,943,633

All of the purchases of shares noted above were made under the Company's Stock Repurchase Program on the open market at prevailing prices using the Company's available cash. The Stock Repurchase Program was announced on December 21, 2005. In February 2008, the Company's Board of Directors authorized an increase in the Stock Repurchase Program, initially approved in December 2005 at \$15.0 million, to \$40.0 million. The program was suspended in May 2008 as a result of the Company's decision to acquire Excel.

***NASDAQ Listing Requirements***

As of the date of this Annual Report on Form 10-K, the Company was subject to the listing requirements of the NASDAQ Global Select Market. Subsequently, however, and as described earlier in this Annual Report on Form 10-K, NASDAQ has determined to delist the Company's shares. The Company's shares are currently quoted on the Pink OTC Markets Inc., continuing under the trading symbol GSIQ.

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*Performance Graph*

The following graph compares the cumulative total return to stockholders for the Company's common shares for the period from December 31, 2003 through December 31, 2008 with the NASDAQ Composite Index and the Philadelphia Semiconductor Index. The comparison assumes an investment of \$100 is made on December 31, 2003 in the Company's common shares and in each of the indices and in the case of the indices it also assumes reinvestment of all dividends. The performance shown is not necessarily indicative of future performance.

**Table of Contents****Item 6. Selected Financial Data**

The consolidated balance sheet as of December 31, 2007 and the consolidated statements of operations for the years ended December 31, 2007 and 2006 have been restated as set forth in this Annual Report on Form 10-K for the year ended December 31, 2008. The data for the consolidated balance sheets as of December 31, 2006, 2005 and 2004 and the consolidated statements of operations for the years ended December 31, 2005 and 2004 have been restated to reflect the impact of the adjustments from the Revenue Review, other adjustments which had been previously identified but not previously recorded due to their materiality, and adjustments to our provision for income tax, but such restated data have not been audited and is derived from the books and records of the Company. The information set forth below is not necessarily indicative of results of future operations, and should be read in conjunction with Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations and the consolidated financial statements and related notes thereto included in Item 8 of this Annual Report on Form 10-K to fully understand factors that may affect the comparability of the information presented below. The information presented in the following tables has been adjusted to reflect the restatement of the Company's financial results, which is more fully described in the Explanatory Note immediately preceding Part I, Item 1 and in Note 2, Restatement of Previously Issued Financial Statements, in the Notes to Consolidated Financial Statements of this Annual Report on Form 10-K. The selected consolidated financial data in this section is not intended to replace the consolidated financial statements.

On November 20, 2009, the Company, along with two of its subsidiaries, voluntarily filed petitions for relief under Chapter 11 of the United States Bankruptcy Code. Under the Bankruptcy Code, the Company's status as a bankruptcy debtor automatically accelerates the payment of all of the Company's debt, including the debt arising under the Senior Notes. Accordingly, the Company has classified this debt as current. These conditions raise substantial doubt about the Company's ability to continue as a going concern, including uncertainty with respect to the realization of the value of its assets and its ability to discharge its liabilities. The consolidated financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classification of liabilities that may result from the outcome of this uncertainty.

	2008	Years Ended December 31,			2004
		2007	2006	2005	
		(In thousands, except per share data)			
		(As Restated)	(As Restated)	(As Restated)	(As Restated)
				(Unaudited)	(Unaudited)
<b>Condensed Consolidated Statements of Operations:</b>					
Sales	\$ 288,468	\$ 291,081	\$ 259,030	\$ 248,283	\$ 319,508
Gross profit	97,618	113,133	102,398	98,239	130,209
Operating expenses:					
Research and development and engineering	33,449	29,861	30,130	25,460	23,928
Selling, general and administrative	65,904	59,545	62,893	58,681	56,839
Amortization of purchased intangible assets	5,714	2,213	2,131	1,971	2,458
Impairment of goodwill, intangible assets and other long-lived assets	215,051				
Restructuring and other	10,485	6,655		212	573
Acquisition related in-process research and development charge	12,142				390
Total operating expenses	342,745	98,274	95,154	86,324	84,188
Income (loss) from operations	(245,127)	14,859	7,244	11,915	46,021
Interest and other income (expense), net	(6,754)	7,313	2,526	1,938	(242)
Income (loss) from continuing operations before income taxes	(251,881)	22,172	9,770	13,853	45,779

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	2008	Years Ended December 31,			2004
		2007	2006	2005	
		(In thousands, except per share data)			
		(As Restated)	(As Restated)	(As Restated)	(As Restated)
				(Unaudited)	(Unaudited)
Income tax provision (benefit)	(39,032)	7,484	2,914	(4,371)	8,481
Net income (loss) from continuing operations	(212,849)	14,688	6,856	18,224	37,298
Income (loss) from discontinued operations, net of tax	270	467	645	(445)	(925)
Gain on disposal of discontinued operations, net of tax	8,732				
<b>Net income (loss)</b>	<b>\$ (203,847)</b>	<b>\$ 15,155</b>	<b>\$ 7,501</b>	<b>\$ 17,779</b>	<b>\$ 36,373</b>
Net income (loss) from continuing operations per common share:					
Basic	\$ (4.94)	\$ 0.35	\$ 0.16	\$ 0.44	\$ 0.91
Diluted	\$ (4.94)	\$ 0.34	\$ 0.16	\$ 0.44	\$ 0.89
Net income (loss) from discontinued operations per common share:					
Basic	\$ 0.21	\$ 0.01	\$ 0.02	\$ (0.01)	\$ (0.02)
Diluted	\$ 0.21	\$ 0.01	\$ 0.02	\$ (0.01)	\$ (0.02)
Net income (loss) per common share:					
Basic	\$ (4.73)	\$ 0.36	\$ 0.18	\$ 0.43	\$ 0.89
Diluted	\$ (4.73)	\$ 0.35	\$ 0.18	\$ 0.43	\$ 0.87
Weighted average common shares outstanding for basic net income (loss) per common share					
	43,125	42,364	41,896	41,548	41,124
Weighted average common shares outstanding for diluted net income (loss) per common share					
	43,125	42,645	42,251	41,856	42,125
	2008	2007	December 31, 2006	2005	2004
			(In thousands)		
		(As Restated)	(As Restated)	(As Restated)	(As Restated)
<b>Balance Sheet Data:</b>					
Cash, cash equivalents and short-term investments	\$ 69,001	\$ 172,387	\$ 136,501	\$ 93,643	\$ 85,043
Debt	185,115				
Working capital (deficit)	(7,434)	267,062	232,427	202,798	162,054
Total assets	520,317	507,645	464,143	397,100	398,326
Deferred revenue, current and long-term	84,225	101,563	80,283	36,511	30,411
Long-term liabilities, excluding deferred revenue	45,820	20,262	25,734	25,577	23,607
Total stockholders' equity	152,677	345,678	317,676	295,753	286,446

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### **Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations**

*Management's Discussion and Analysis of Financial Condition and Results of Operations ( MD&A ) should be read in conjunction with the Consolidated Financial Statements and Notes included in Item 8 of this Annual Report on Form 10-K. The MD&A contains certain forward-looking statements within the meaning of the United States Private Securities Litigation Reform Act of 1995, Section 27A of the United States Securities Act of 1933, as amended, and Section 21E of the United States Securities Exchange Act of 1934, as amended. In addition to historical financial information, the following discussion and analysis contains forward-looking statements that involve risks, uncertainties and assumptions. These forward-looking statements include, but are not limited to, anticipated financial performance; anticipated outcome of the Chapter 11 Cases; the impact of our delisting from NASDAQ; our ability to continue as a going concern; expected liquidity and capitalization; drivers of revenue growth; management's plans and objectives for future operations, expenditures and product development and investments in research and development; business prospects; potential of future product releases; anticipated sales performance; industry trends; market conditions; changes in accounting principles and changes in actual or assumed tax liabilities; expectations regarding tax exposure; expectations related to the restructuring of our debt through the Chapter 11 Cases; anticipated reinvestment of future earnings; anticipated expenditures in regard to the Company's benefit plans; future acquisitions and dispositions and anticipated benefits from prior acquisitions; anticipated outcomes of legal proceedings and litigation matters; and anticipated use of currency hedges. These forward-looking statements are neither promises nor guarantees, but involve risks and uncertainties that may cause actual results to differ materially from those contained in the forward-looking statements. Our actual results could differ materially from those anticipated in these forward-looking statements for many reasons, including the risks described in Item 1A of this Annual Report on Form 10-K and elsewhere in this Annual Report on Form 10-K. See also Cautionary Statement Regarding Forward-Looking Statements at the beginning of this Annual Report on Form 10-K. Readers should not place undue reliance on any such forward-looking statements, which speak only as of the date they are made. Management and the Company disclaim any obligation to publicly update or revise any such statement to reflect any change in its expectations or in events, conditions, or circumstances on which any such statements may be based, or that may affect the likelihood that actual results will differ from those contained in the forward-looking statements.*

### **Business Overview**

We design, develop, manufacture and sell photonics-based solutions (consisting of lasers, laser systems and electro-optical components), precision motion devices, associated precision motion control technology and systems. Our customers incorporate our technology into their products or manufacturing processes, for a wide range of applications in the industrial, scientific, electronics, semiconductor, medical and aerospace markets. Our products allow customers to make advances in materials and processing technology and to meet extremely precise manufacturing specifications, including device complexity and miniaturization.

The photonics and electro-optical industry is subject to intense competition and rapid technological developments. Our strength and success is dependent upon developing and delivering successful, timely and cost effective solutions to our customers. For us to maintain our performance, we believe we must continue to increase our operational efficiencies, improve and refine our existing products, expand our product offerings and develop new applications for our technology.

The Company strives to create shareholder value through:

Organic sales growth by delivering a consistent stream of successful new product launches,

Generating high levels of cash flow from operations, and

Acquiring and successfully integrating businesses that have complementary and established core competencies.

We and our subsidiaries serve three primary industries or market segments: Precision Technology, Semiconductor Systems, and Excel. The Company's Precision Technology Segment primarily sells components to original equipment manufacturers (OEMs), who then integrate its products into application specific products or systems. The Company's OEM products include those based on its core competencies in laser, precision motion and motion control technology. The Company's Semiconductor Systems Segment designs, develops and sells production systems that process semiconductor wafers using laser beams and high precision motion technology. The Company sells manufacturing systems to integrated device manufacturers and wafer processors. The Company's Excel Segment designs, manufactures and markets photonics-based solutions consisting of lasers, laser-based systems, precision motion devices and electro-optical components, primarily for industrial and scientific applications. The Company's Excel Segment primarily sells components to OEMs, who then integrate its products into application specific products or systems.

**Strategy**

GSI strives to expand its presence in its most attractive markets both through organic growth and strategic acquisitions. This strategy led to our acquisition of Excel in the third quarter of 2008. This transaction was a major step for us, as it introduced us to

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some of the attractive markets in which the Excel Segment operates, and it expanded our presence in some of the most attractive markets in which the Precision Technology Segment operates. During 2008 and 2009, we initiated the integration of Excel's operations with ours. In 2010, we intend to focus on the completion of the integration of Excel into our operations and on the continued development and introduction of new products. In addition, we intend to continue to explore potential divestments of non-strategic businesses.

We had a number of significant events in 2008, and also in 2009 and 2010 through the filing of this Annual Report on Form 10-K. Discussion of those events follows.

### Significant Events in 2008

Financial data, when presented throughout MD&A and our accompanying consolidated financial statements, includes the effect of each of the following:

1. **Restatement of our Financial Results.** This restatement is more fully described in the Explanatory Note immediately preceding Item 1 of this Annual Report on Form 10-K, and in Note 2, Restatement of Previously Issued Financial Statements, in Notes to Consolidated Financial Statements. The following table presents revenues and deferred revenues as reported and as restated (in thousands):

	Year Ended December 31,				
	2008	2007	2006	2005	2004
				(unaudited)	(unaudited)
<b>Revenues:</b>					
As reported (a)	\$ 288,468	\$ 306,067	\$ 302,083	\$ 251,761	\$ 321,367
As restated		291,081	259,030	248,283	319,508
<b>Deferred Revenue (b):</b>					
As reported (a)	\$ 84,225	\$ 9,949	\$ 2,965	\$ 2,963	\$ 1,811
As restated		101,563	80,283	36,511	30,411

- (a) Excludes U.S. Optics Business which is classified as discontinued operations.  
 (b) Includes current and non-current deferred revenue.

2. **Divestiture of our U.S. Optics Business.** In October 2008, we sold our U.S. Optics Business which was located in Moorpark, California, and which was historically included in our Precision Technology Segment. On October 8, 2008, we completed the sale of our U.S. Optics Business for \$21.6 million. The net gain of \$8.7 million on the sale of this business is reported as Gain on Disposal of Discontinued Operations, net of tax, in our consolidated statements of operations. This sale is more fully described in Note 5, Discontinued Operations, in Notes to Consolidated Financial Statements of this Annual Report on Form 10-K.
3. **Excel Acquisition.** In August 2008, we completed our acquisition of Excel, a designer, manufacturer and marketer of photonics-based solutions consisting of lasers, laser based systems, precision motion devices and electro-optical components, primarily for industrial and scientific applications. Excel has complementary products, technologies, and distribution channels to ours that we believe will enable us to provide customers with a significantly broader set of technical solutions and to expand our market share. The Excel acquisition had a material impact on our results of operations in 2008. Excel was included in our consolidated financial statements since August 20, 2008. See Note 4, Business Combinations, of Notes to Consolidated Financial Statements of this Annual Report on Form 10-K for details. The material impact on our financial results includes the normal operations since August 20, 2008, and also includes an impairment charge with respect to a portion of the goodwill, intangible assets and other long-lived assets that we acquired in our purchase of Excel.





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4. ***Debt Financing.*** We financed the purchase price of Excel in part from the net proceeds that were received from our sale of \$210.0 million of senior unsecured notes and warrants to purchase our common shares. The remaining cash required to acquire Excel was provided by cash on hand at the time of closing.
5. ***Impairment of Goodwill, Intangible Assets and Other Long-lived Assets.*** We recorded a charge of \$215.1 million relating to our assessment of the fair value of these assets as of December 31, 2008. This charge includes a portion of the assets that we acquired from Excel in August 2008, and is more fully discussed below under Significant Accounting Policies and Estimates, and also in Note 3 of Notes to Consolidated Financial Statements of this Annual Report on Form 10-K.
6. ***Restructuring Charges.*** In 2008, we recorded restructuring and other charges of \$10.5 million relating to a number of initiatives to reduce our workforce, the cessation or relocation of certain activities, and our Revenue Review and related restatement of historic financial statements. These activities are discussed further, below, in our discussion of our results of operations for the years ended December 31, 2008 and 2007.

### **Significant Events in 2009**

In 2009, the Company had a number of significant developments. Certain of these developments are discussed in Item 1, Significant Recent Developments of this Annual Report on Form 10-K under the following headings: NASDAQ Delisting Determination, Chapter 11 Bankruptcy Filing, The Third Modified Joint Chapter 11 Plan of Reorganization, The Plan Support Agreement, and SEC Investigation.

In addition to these events, we also undertook a number of restructuring activities in 2009. We undertook a number of cost reduction initiatives, including a workforce reduction of approximately 214 employees in fiscal 2009. The total approximate severance paid in 2009 by the Company in connection with these initiatives was approximately \$3.9 million. The approximate annualized savings realized by us from these workforce reductions was approximately \$11.2 million.

Our Revenue Review and related restatement of historic financial statements has continued into 2009 as well. The costs for these activities are significant, and will be charged to restructuring and other costs as incurred.

### **Going Concern**

As a result of certain of the significant events discussed above and uncertainties inherent in the bankruptcy process, there is substantial doubt about our ability to continue as a going concern. Operating in bankruptcy imposes significant risks and uncertainties on our business. See Item 1A Risk Factors Risks Relating to Bankruptcy for a discussion of the risks and uncertainties relating to our business and investing in our securities as a result of the Chapter 11 Cases.

We believe that when we emerge from bankruptcy, we will be sufficiently capitalized. We expect that we will have assets that exceed our liabilities, and that those assets, as well as the net assets derived from our continuing operations, will be sufficient to meet our obligations, including the obligations with respect to the payment of interest, and repayment of principal under the New Term Loan. Notwithstanding our expectation upon our emergence from bankruptcy, uncertainties inherent in the bankruptcy process raise substantial doubt about our ability to continue as a going concern. In particular, until the Plan is confirmed by the Court, we may be required to pay the Senior Note Claims under the original terms of the Senior Notes. The consolidated financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classification of liabilities that may result from the outcome of this uncertainty.

### **Overview of Financial Results**

As a result of the significant events discussed above, our financial results in 2008 differ significantly from those in recent years. We reported a net loss of \$203.8 million in 2008, compared to net income of \$15.2 million in 2007 and net income of \$7.5 million in 2006. Our 2008 operating results included three significant non-recurring charges: we recorded a charge of \$215.1 million relating to the impairment of our goodwill, intangible assets and other long-lived assets; we expensed \$12.1 million of acquisition related in-process research and development in connection with our acquisition of Excel; and we expensed \$10.5 million in connection with restructuring and other non-recurring activities.

The financial results of 2008 reflect the extremely difficult global economic environment, which resulted in significantly weakened demand for our products, which ultimately resulted in our recording of a loss of \$203.8 million in 2008. The



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specific components of our loss, and enhanced discussion of the factors that led to this loss are further discussed below in the comparison of our 2008 and 2007 financial results. During the first half of 2009, the Company experienced further deterioration in both its sales and operating profits. Sales declined across the Precision Technology and Semiconductor Segments; Excel was not owned in the first half of 2008. Sales in the Company's Semiconductor Systems Segment underwent a particularly pronounced decline, as the semiconductor industry went through one of the worst downturns in the industry's history. Overall sales recovered somewhat later in 2009. The Company's business outlook for 2010 remains uncertain.

**Table of Contents****Results of Operations**

The following table sets forth our results of operations as a percentage of sales for the periods indicated:

	2008	Year Ended December 31, 2007 (As Restated)	2006 (As Restated)
Sales	100.0%	100.0%	100.0%
Cost of goods sold	66.2	61.1	60.5
<b>Gross profit</b>	<b>33.8</b>	<b>38.9</b>	<b>39.5</b>
Operating expenses:			
Research and development and engineering	11.6	10.3	11.6
Selling, general and administrative	22.8	20.5	24.3
Amortization of purchased intangible assets	2.0	0.8	0.8
Impairment of goodwill, intangible assets and other long-lived assets	74.5		
Restructuring and other	3.7	2.3	
Acquisition related in-process research and development charge	4.2		
<b>Total operating expenses</b>	<b>118.8</b>	<b>33.9</b>	<b>36.7</b>
Income (loss) from operations	(85.0)	5.0	2.8
Interest income	1.1	2.2	1.8
Interest expense	(3.6)		(0.2)
Foreign exchange transaction gains (losses)	0.3	0.2	(0.6)
Other income (expense), net	(0.2)	0.1	
<b>Income (loss) from continuing operations before income taxes</b>	<b>(87.4)</b>	<b>7.5</b>	<b>3.8</b>
Income tax provision (benefit)	(13.5)	2.6	1.1
<b>Income (loss) from continuing operations</b>	<b>(73.9)</b>	<b>4.9</b>	<b>2.7</b>
Income from discontinued operations, net of tax		0.2	0.2
Gain on disposal of discontinued operations, net of tax	3.1		
<b>Net income (loss)</b>	<b>(70.8)%</b>	<b>5.1%</b>	<b>2.9%</b>

**Table of Contents****Years Ended December 31, 2008 and 2007****Sales**

The following table sets forth sales by business segment for 2008 and 2007 in dollars (dollars in thousands) and percentage change:

	2008	2007 (As Restated)	Increase (Decrease)	Percentage Change
Precision Technology	\$ 146,616	\$ 184,509	\$ (37,893)	20.5%
Semiconductor Systems	88,494	111,515	(23,021)	(20.6)%
Excel	55,612		55,612	100.0%
Intersegment sales eliminations(1)	(2,254)	(4,943)	2,689	(54.4)%
<b>Total</b>	<b>\$ 288,468</b>	<b>\$ 291,081</b>	<b>\$ (2,613)</b>	<b>(0.9)%</b>

(1) Sales of the Precision Technology Segment's products to the Semiconductor Systems Segment.

Precision Technology product lines' sales decreased by \$37.9 million, or 20.5%, in 2008. The decrease in sales of these product lines was primarily attributable to declines in our Spindles and Encoders product lines in the second half of 2008. Worldwide demand for those products and in general weakened markedly in late 2008 as turmoil in world financial markets intensified, credit conditions tightened and business and consumer confidence plummeted. The weakness in demand continued during the first half of 2009 before starting to recover late in 2009.

The decrease in Semiconductor Systems sales was primarily attributable to the global slowdown which had a dramatic adverse effect on the semiconductor market, which saw a markedly weakened end-user market for products. This weakened end-user demand directly affected our customers' purchases of equipment that is used to produce semiconductor products. Included in the 2008 revenue is revenue from many orders that were placed by customers prior to 2008, but that were not able to be fully delivered in those prior periods. The revenue has been recorded in 2008, upon our completion of all deliverables for this equipment. Our worldwide deferred revenue is primarily related to our Semiconductor Systems. It decreased 17.1% from \$101.6 million at December 31, 2007 to \$84.2 million at December 31, 2008. We expect that a significant portion of the deferred revenue relating to undelivered elements as of December 31, 2008 will be recognized in 2009 and 2010. The decrease in sales of Semiconductor Systems was particularly pronounced in the second half of 2008. Sales of Semiconductor Systems continued at a low level throughout most of 2009. The outlook for 2010 is uncertain.

Excel contributed sales of \$55.6 million from the date of acquisition in August 2008 to December 31, 2008.

We measure the sales to our customers based on the geographic location of each customer. Based on these locations, \$88.5 million and \$79.2 million, or 30.7% and 27.2%, of our total sales were made to customers in the United States in 2008 and 2007, respectively. Our sales to customers outside of the United States represented \$199.9 million and \$211.9, or 69.3% and 72.8%, of our total sales in 2008 and 2007, respectively. The difference in proportion of our sales derived from customers within the United States is primarily attributable to our acquisition of Excel in August 2008, as Excel has a higher proportion of its revenue demand from customers located in the United States.

**Table of Contents***Gross Profit*

The following table sets forth gross profit and gross profit percentage, by business segments for 2008 and 2007 (dollars in thousands):

	2008	2007 (As Restated)
<b>Gross profit:</b>		
Precision Technology	\$ 49,092	\$ 66,877
Semiconductor Systems	27,523	45,958
Excel	20,669	
Intersegment sales elimination and other	334	298
<b>Total</b>	<b>\$ 97,618</b>	<b>\$ 113,133</b>
<b>Gross profit percentages:</b>		
Precision Technology	33.5%	36.2%
Semiconductor Systems	31.1%	41.2%
Excel	37.2%	
Intersegment sales elimination and other	(14.8)%	(6.0)%
<b>Total</b>	<b>33.8%</b>	<b>38.9%</b>

Gross profit as a percentage of sales can be influenced by a number of factors including product mix, pricing, volume, costs for raw materials and outsourced manufacturing, warranty costs and charges related to excess and obsolete inventory, at any particular time.

The Precision Technology Segment gross profit margins were 33.5% in 2008, a decrease of 2.7 percentage points compared to 36.2% in 2007. The decline of gross profit is primarily due to changes in product mix, as the gross profits vary among the product lines in this segment.

The Semiconductor Systems Segment gross profit reduction of 10.1 percentage points is primarily attributable to fixed costs being absorbed into the revenue base that decreased by 20.6% in 2008 as compared to 2007.

The gross profit margins of the products within the Excel Segment were 37.2% in 2008 since the date of acquisition in August 2008.

*Research and Development and Engineering Expenses*

Research and development and engineering ( R&D ) expenses are primarily comprised of labor and other employee-related expenses. R&D expenses were \$33.4 million in 2008, representing 11.6% of sales compared to \$29.9 million, or 10.3%, of sales in 2007. R&D expenses, in terms of their total dollars, primarily increased as a result of our acquisition of Excel in August 2008. The increases in R&D expenses were partially offset by our 2008 reductions in force in connection with restructuring activities discussed below. We believe that the development and market introduction of new products and the enhancement of existing products are essential to our success. Accordingly, during 2009, we continued to invest in the development of new products across all three of our segments. We plan to continue to invest in R&D as we continue to pursue market leadership in all of our segments.

*Selling, General and Administrative Expenses*

Selling, general and administrative ( SG&A ) expenses include costs for sales and marketing, sales administration, finance, human resources, legal, information systems, facilities and executive management, and includes personnel related costs, commissions, advertising, legal, tax, accounting and other professional fees. SG&A expenses were \$65.9 million in 2008, representing 22.8% of sales, compared to \$59.5 million, or 20.5% of sales in 2007. SG&A expenses, in terms of their total dollars, increased primarily as a result of personnel related costs associated with our acquisition of Excel in August 2008. The increases were partially offset by reductions in payroll related costs attributable to our 2008 reductions in force in connection with restructuring activities discussed below. Additionally, in 2007, we recorded a \$2.0 million reduction to our SG&A expenses due to the cash payment we received in connection with the settlement of our claims against Lumenis Ltd.



**Table of Contents***Amortization of Purchased Intangible Assets*

Amortization of intangible assets is discussed below in Critical Accounting Policies and Estimates. Amortization of purchased intangible assets is charged to our Precision Technology and Excel Segments. Amortization of purchased intangible assets, excluding the amortization for core technology that is included in cost of goods sold, was \$5.7 million, or 2.0% of sales in 2008, compared to \$2.2 million, or 0.8%, of sales in 2007. The increase in 2008, in terms of dollars and as a percentage of sales, was primarily related to the amount of intangible assets acquired in connection with our acquisition of Excel in August 2008.

As discussed below, on December 31, 2008, we recorded a \$215.1 million charge for the impairment of goodwill, intangible assets and other long-lived assets. Based on the amortizable intangible assets as of December 31, 2008, and assuming no impairment or reduction in the expected lives, we expect to record amortization of intangible assets for 2009 of \$9.6 million, of which \$3.8 million will be recorded to cost of goods sold, and \$5.8 million will be recorded to SG&A expenses.

*Impairment of Goodwill, Intangible Assets and other Long-Lived Assets*

As of December 31, 2008, we conducted a review to assess whether the carrying value of our goodwill, intangible assets and other long-lived assets was impaired. Based on our review, we noted that the carrying value of certain assets exceeded their fair market value. Additional information with respect to the manner in which we conducted our review is discussed below under Critical Accounting Policies and Estimates. Based on our evaluation, we recorded a charge to reduce the carrying amounts of goodwill, intangible assets and other long-lived assets by an aggregate of \$215.1 million.

*Restructuring and other*

We recorded restructuring and other charges of \$10.5 million and \$6.7 million in 2008 and 2007, respectively. In 2008, we reported charges of \$3.6 million in connection with our closure of excess manufacturing operations in the United Kingdom, as those operations moved to China. We also accrued \$4.7 million to consolidate certain of our operations within the United States, including charges for duplicate facilities and staffing reductions, into our new Bedford, Massachusetts facility. These 2008 charges were partially offset by reductions to the restructuring charge relating to the sale of inventory at a price that exceeded the value that such inventory had been written down to in a prior year's restructuring charge. The 2008 restructuring and other costs also include \$1.9 million relating to our Revenue Review. This amount includes amounts payable to third parties, including attorneys, forensic accountants, and other advisors. These costs have been charged to expense as incurred. The Revenue Review costs, including costs relating to the restatement of historic financial statements, have continued for periods subsequent to 2008, and will be included in future restructuring and other charges.

The 2007 charges related primarily to a charge of \$6.7 million relating to our expansion of certain manufacturing operations in China. The charge was composed of \$2.6 million in employee termination benefits, \$3.1 million in inventory write-offs, \$0.7 million in direct costs associated with the manufacturing transition from the United Kingdom to China, and \$0.3 million related to facility consolidations. The inventory write-offs were charged to restructuring and other charges as they related to discontinued product offerings, and not recurring activities. These restructuring efforts were largely completed in 2007.

The following table summarizes the aggregate balance of the activity relating to our restructuring and other charges recorded on our consolidated balance sheets (in thousands):

Balance at December 31, 2005	\$ 1,502
Restructuring charges (benefits), net	
Cash payments	(165)
Balance at December 31, 2006	1,337
Restructuring charges (benefits), net	6,655
Cash payments	(3,249)
Non-cash write-offs or other adjustments	(3,401)
Balance at December 31, 2007	1,342
Restructuring charges (benefits), net	10,485



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Cash payments	(4,223)
Non-cash write-offs or other adjustments	(3,563)
Balance at December 31, 2008	\$ 4,041

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As of December 31, 2008 and 2007, \$1.1 million and \$1.0 million, respectively, of accrued restructuring charges were included in long-term liabilities. The current portion is included in accrued expenses (see Note 7 of Notes to Consolidated Financial Statements).

*Acquisition Related In-Process Research and Development Charge*

In connection with our acquisition of Excel in August 2008, we recorded a \$12.1 million charge for acquisition related in-process research and development. The value assigned to in-process research and development was determined using an income approach by estimating the costs to develop the acquired technology into commercially viable products, estimating the resulting net cash flows from the projects, and discounting the net cash flows to their present value. At the date of acquisition, the development of these projects had not yet reached technological feasibility, and had no alternative future uses. Accordingly, we have expensed the value of this research and development at the acquisition date in accordance with the provisions of Statement of Financial Accounting Standards ( SFAS ) 141. Due to the nature of the forecasts and the risks associated with the developmental projects, a discount rate of 15.0% was used to discount the net cash flows to their present value. We anticipate that costs to complete the development of these projects will be \$4.4 million, and will be completed between December 2008 and December 2010. The successful development of new products and product enhancements is subject to numerous risks and uncertainties, both known and unknown, including unanticipated delays, access to capital, budget overruns, technical problems and other difficulties that could result in the abandonment or substantial change in the design, development and commercialization of these new products and enhancements. Given the uncertainties inherent with product development and introduction, there can be no assurance that any of our product development efforts will be successful on a timely basis or within budget, if at all. The failure of the combined Company to develop new products and product enhancements on a timely basis or within budget could harm our results of operations and financial condition.

*Interest Income*

Interest income was \$3.3 million in 2008, compared to \$6.6 million in 2007. Interest income decreased primarily due to us having lower cash and investment balances following our acquisition of Excel in August 2008.

*Interest Expense*

Interest expense was \$10.4 million in 2008, compared to \$0.1 million in 2007. Interest expense increased due to us having incurred \$210.0 million in debt, the proceeds of which were used to fund a portion of the purchase of our acquisition of Excel in August 2008.

*Foreign Exchange Transaction Gains (Losses)*

Foreign exchange currency transaction gains, net, were \$0.9 million in 2008, compared to \$0.6 million in 2007, which arose from the change in exchange rates from 2008 compared to 2007, and which resulted in additional other income of \$0.3 million in 2008 compared to 2007.

*Other Income (Expense), Net*

Other income (expense), net, was \$(0.6) million in 2008 as compared to \$0.2 million in 2007. The difference is primarily attributable to a penalty that we recorded in 2008 relating to our inability to maintain the effectiveness of the registration statement on Form S-3 that we filed in October 2008 relating to the resale of our common shares issued upon the exercise of the Warrants. See Note 8 of Notes to Consolidated Financial Statements. We did not have any such charge in 2007.

*Income Taxes*

The Company recorded a tax benefit of \$39.0 million during the 2008 fiscal year. The effective tax rate for 2008 was (15.5%) of income before taxes, compared to an effective tax rate of 33.8% of income before taxes for 2007. The Company is incorporated in Canada and therefore uses the Canadian statutory rate. The Company's tax rate in 2008 differs from the Canadian statutory rate of 29.5% primarily due to a \$47.0 million charge for unfavorable permanent differences of

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which \$43.0 million relates to non-deductible amortization and \$4.3 million to in-process R&D, \$1.8 million related to Canadian deferred items, a \$0.4 million charge for non-U.S. withholding taxes, a \$1.1 million increase in the Company's liability for uncertain tax positions, \$0.5 million increase in valuation allowance in the U.S., and a \$1.6 million increase in valuation allowance due to restatement and impairment in the U.K. The aforementioned charges were partially offset by benefits derived from \$0.2 million benefit from R&D tax credits, \$0.5 million decrease in valuation allowance in Hong Kong, \$1.7 million related to the release of valuation allowances in Canada due to the utilization of net operating losses against the current year income in Canada and \$13.9 million benefit due to international rate differences.

In connection with the Chapter 11 Cases described in Note 1 of Notes to Consolidated Financial Statements, the IRS has filed amended proofs of claim aggregating approximately \$7.7 million for amounts it claims the Company owes for 2002 through 2008. The IRS has provided no information to substantiate its claims. The Company believes the IRS claims are without merit and intends to vigorously object to them in Bankruptcy Court. Consequently, the Company believes no adjustment of its estimated tax liability pursuant to FIN 48 is required.

*Income from Discontinued Operations, Net of Tax*

On October 8, 2008, we completed the sale of our U.S. Optics Business, located in Moorpark, California, which was a part of our Precision Technology Segment, for proceeds of \$21.6 million. The net gain of \$8.7 million on the sale of the U.S. Optics Business is reported as Gain on Disposal of Discontinued Operations, net of tax, in our consolidated statements of operations for the year ended December 31, 2008. The operating results of this business have been reclassified and reported as income from discontinued operations in our consolidated statements of operations for fiscal years 2008, 2007 and 2006.

*Years Ended December 31, 2007 and 2006**Sales*

The following table sets forth sales by business segment for 2007 and 2006 in dollars (dollars in thousands) and percentage change:

	2007 (As Restated)	2006 (As Restated)	Increase (Decrease)	Percentage Change
Precision Technology	\$ 184,509	\$ 179,565	\$ 4,944	2.8%
Semiconductor Systems	111,515	90,170	21,345	23.7%
Intersegment sales eliminations(1)	(4,943)	(10,705)	5,762	(53.8)%
Total	\$ 291,081	\$ 259,030	\$ 32,051	12.4%

(1) Sales of the Precision Technology Segment's products to the Semiconductor Systems Segment.

The increase in sales of our Precision Technology Segment was primarily attributable to our PCB spindles product line, and our Optics product line, which includes revenue from the beryllium mirror and structures business of the U.K.-based Thales Optronics that we acquired in June 2007. Additionally, in 2007 we recognized \$7.3 million relating to shipments that we made to a customer from 2004 to 2007. Those shipments were only able to be recognized as revenue upon finalization of our arrangement with that customer. These increases in revenue for the Precision Technology Segment were partially offset by (i) a reduction in sales of our Thermal Printer products due to reduced shipments to a large medical defibrillator customer that voluntarily suspended U.S. shipments to address quality systems issues in their manufacturing facility and (ii) reductions in sales of our Scanner and Laser product lines.

The increase in Semiconductor Systems sales were primarily attributable to aggressive semiconductor capital spending by our customers that began in 2006 and continued into early 2007. In particular, we experienced strong demand for our WaferMark equipment, particularly from the manufacturers of semiconductor products who increased production capacity to meet consumer demand for DRAM and Flash memory, as well as increased demand for our WaferRepair equipment, including orders for our M450 series in 2006, and our M550 series that became available in early 2007. In many cases, the orders for the M450 series of WaferRepair systems were fulfilled, installed and then recognized as revenue in 2007. Despite the volume of new orders in 2007 for our M550 series equipment, most of these M550 series equipment orders were not able to be fully deployed in 2007 and had undelivered commitments against some aspect of the equipment ordered. As a result, many of these orders were

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included in our deferred revenue as of December 31, 2007. Our worldwide deferred revenue is primarily related to sales in our Semiconductor Systems, and increased from \$80.3 million at December 31, 2006 to \$101.6 million at December 31, 2007, due in large part to the deferral of revenue related to orders for our M550 series products.

We track the sales to our customers based on the geographic location of each customer. Based on these locations, \$79.2 million and \$82.7 million, or 27.2% and 31.9% of our total sales were made to customers in the United States in 2007 and 2006, respectively. Our sales to customers outside of the United States represented \$211.9 million and \$176.3 million, or 72.8% and 68.1% of our total

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sales in 2007 and 2006, respectively. The proportional increase in customer sales outside of the United States was primarily due to our 2007 increase in sales to Semiconductor Systems customers, which customers are largely located outside of the United States, where their production factories are primarily located.

*Gross Profit*

The following table sets forth gross profit and gross profit percentage, by our business segments for 2007 and 2006 (dollars in thousands):

	2007 (As Restated)	2006 (As Restated)
Gross profit:		
Precision Technology	\$ 66,877	\$ 68,224
Semiconductor Systems	45,958	34,198
Intersegment sales elimination and other	298	(24)
<b>Total</b>	<b>\$ 113,133</b>	<b>\$ 102,398</b>
Gross profit percentage:		
Precision Technology	36.2%	38.0%
Semiconductor Systems	41.2%	37.9%
Intersegment sales elimination and other	(6.0)%	0.2%
<b>Total</b>	<b>38.9%</b>	<b>39.5%</b>

Gross profit as a percentage of sales can be influenced by a number of factors including product mix, pricing, volume, costs for raw materials and outsourced manufacturing, warranty costs and charges related to excess and obsolete inventory, at any particular time.

The decline in gross profit of our Precision Technology Segment of 1.8 percentage points was largely due to changes in product mix, as gross profit varies among the product lines in this segment. The Semiconductor Systems Segment saw gross profit increase by 3.3 percentage points in 2007. This increase in gross profit in the Semiconductor Systems Segment is largely the result of fixed costs being absorbed into a larger revenue base in 2007, as compared to 2006.

*Research and Development and Engineering Expenses*

Research and development and engineering ( R&D ) expenses are primarily comprised of labor and other employee-related expenses. R&D expenses were \$29.9 million in 2007, representing 10.3% of sales, compared to \$30.1 million, or 11.6%, of sales in 2006. Although R&D expenses were relatively consistent in 2007 and 2006, R&D expenses as a percentage of revenue decreased in 2008 because sales in 2007 increased relative to sales in 2006, thereby spreading the relatively unchanged dollars dedicated to R&D over a larger base of sales.

*Selling, General and Administrative Expenses*

Selling, general and administrative ( SG&A ) expenses includes costs for sales and marketing, sales administration, finance, human resources, legal, information systems, facilities and executive management, and includes personnel related costs, commissions, advertising, legal, tax, accounting and other professional fees. SG&A expenses were \$59.5 million in 2007, representing 20.5% of sales, compared to \$62.9 million, or 24.3%, of sales in 2006. The SG&A expenses decreased in 2007 relative to 2006, primarily due to us having recorded a \$2.0 million reduction to our SG&A expenses as a result of the settlement for legal claims, for which the settlement represented a recovery of previously expensed amounts.

*Amortization of Purchased Intangible Assets*

Amortization of intangible assets is discussed below in Critical Accounting Policies and Estimates . Amortization of purchased intangible assets in 2007 and 2006 was charged to our Precision Technology Segment. Amortization of purchased intangible assets, excluding the amortization for core technology that is included in cost of goods sold, was \$2.2 million in 2007 and \$2.1 million in 2006, and was derived from acquisitions that we consummated prior to 2006.

*Restructuring and other*

We recorded restructuring charges of \$6.7 million in 2007, which are discussed above in the comparison of 2008 and 2007 charges. We had no such charges in 2006.

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### *Interest Income*

Interest income was \$6.6 million in 2007, compared to \$4.6 million in 2006. The \$2.0 million increase in 2007 is due to an increase in our invested cash balances in 2006 as compared to 2007, along with a more favorable yield on those balances.

### *Interest Expense*

Interest expense was \$0.1 million in 2007 and \$0.6 million in 2006. The interest expense booked in 2006 was primarily composed of a charge of \$0.5 million relating to a payment to the German tax authorities in 2006 in connection with the closure of a 2005 tax audit.

### *Foreign Exchange Transaction Gains (Losses)*

Foreign exchange currency transaction gains were \$0.6 million in 2007, compared to a \$1.4 million loss in 2006. These amounts arise primarily from transactions denominated in currencies other than the functional currency. The currencies that the gains and losses are primarily derived from are the British Pound, the Japanese Yen and the Canadian Dollar. The U.S. dollar had relative strength to the currencies in 2007 as compared to 2006.

### *Other Income (Expense), Net*

Other income (expense), net, was not significant in either 2007 or 2006, providing \$0.2 million of income and (\$0.1) million of expense, respectively.

### *Income Taxes*

We recorded a tax provision of \$7.5 million during 2007. The effective tax rate for 2007 was 33.8% of income before taxes, compared to an effective tax rate of 29.8% for 2006. Our tax rate in 2007 differs from the Canadian statutory rate of 32.1% due to a \$0.3 million charge for state taxes, a \$0.8 million charge for non-U.S. withholding taxes, a \$0.9 million increase in our liability for uncertain income tax positions, the recording of a \$1.0 million additional valuation allowance in the United Kingdom, the recording of a \$0.7 million additional valuation allowance in the United States. The aforementioned charges were partially offset by a \$0.3 million benefit from research and development tax credits, a \$0.7 million adjustment to prior years' benefits claimed for the extraterritorial income exclusion, and a \$1.3 million release of valuation allowance in Canada due to the utilization of net operating losses against the current year income in Canada.

## **Liquidity and Capital Resources**

On November 20, 2009, GSIG, together with two of its subsidiaries, voluntarily filed petitions for relief under Chapter 11 of the United States Bankruptcy Code. Under the Bankruptcy Code, GSIG's status as a bankruptcy debtor automatically accelerates the payment of all of its debt, including the debt arising under the Senior Notes. Accordingly, this debt has been classified as current. These conditions raise substantial doubt about our ability to continue as a going concern, including uncertainty with respect to the realization of the value of our assets, and our ability to discharge our liabilities. The consolidated financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classification of liabilities that may result from the outcome of this uncertainty.

Cash and cash equivalents totaled \$69.0 million at December 31, 2008, compared to \$172.4 million at December 31, 2007. The decrease in cash and cash equivalents is primarily related to the cash on hand that we used to fund our acquisition of Excel in August 2008.

As of December 31, 2008 we also held auction rate securities, recorded at fair value of \$25.1 million and with a par value of \$32.3 million, which we obtained in connection with our acquisition of Excel. These auction rate securities are student loans backed by the federal government and are privately insured. Current capital market conditions have impacted our ability to liquidate certain auction rate securities. Liquidity for these auction rate securities is typically provided by an auction process that resets the applicable interest rate at pre-determined intervals, usually every 7, 28, 35 or 90 days. In the past, the auction process has allowed investors to roll over their holdings or obtain immediate liquidity by selling the securities at par. Due to the current capital market conditions, auctions have not had sufficient bidders to allow investors to complete a sale of some auction rate securities. Due to the uncertainty in the market as to when these auction rate notes will be refinanced or the auctions will resume, we have classified these instruments as





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long-term assets available for sale. We have had some success in liquidating these holdings during 2009. Through December 31, 2009, of the \$32.3 million in par value securities that we held as of December 31, 2008, we sold \$19.3 million of the securities, and recorded net realized gains of \$2.4 million on our sales of these securities. As of December 31, 2009, the Company continues to hold auction rate securities with a par value of \$13.0 million.

*Cash Flows for the Year Ended December 31, 2008 and December 31, 2007*

Cash provided by operations in 2008 was \$38.9 million, compared to \$37.6 million in 2007, a difference of \$1.3 million or 3.5%. The increase in cash flow was primarily attributable to the following factors:

In 2008, we recorded a net loss of \$203.8 million, compared with net income of \$15.2 million in 2007, before non-cash adjustments to reconcile net income (loss) to net cash from operating activities.

Non-cash adjustments to reconcile net income (loss) to cash flows from operations, including the following material items:

In 2008, we recorded an impairment charge of \$215.1 million to write down our goodwill, other intangible assets and property, plant and equipment to their fair value as of December 31, 2008, and we also recorded an acquisition related in-process research and development charge of \$12.1 million in connection with our acquisition of Excel. There were no such charges recorded in 2007;

Other non-cash charges, such as depreciation and amortization of fixed assets and intangible assets, non-cash restructuring charges, share-based compensation, and non-cash interest accretion charges, were \$27.1 million in 2008 and \$20.3 million in 2007. The \$6.8 million increase in non-cash charges was primarily attributed to an increase in depreciation and amortization of \$4.4 million, and \$1.9 million of non-cash interest expense in 2008; and

In 2008, we recorded a \$33.7 million increase in deferred income taxes, compared with a \$1.1 million decrease in 2007.

Changes in our operating assets and liabilities provided \$31.0 million in cash in 2008, as compared to having provided \$1.6 million in 2007. The significant increase is primarily attributable to the following items:

A decrease in our accounts receivable balances in 2008 provided \$37.8 million, as compared to having used cash of \$20.2 million in 2007;

Inventory balances decreased \$19.9 million in 2008, compared with a \$5.4 million decrease in 2007;

In 2008, the net change to deferred revenue and related deferred cost of goods sold used \$10.2 million, compared to a net increase of \$7.3 million in 2007; and

In 2008, the net cash flows used in accounts payable and accrued expenses was \$8.0 million, as compared to cash flow provided from these activities of \$4.1 million in 2007.

Cash used in operating activities of discontinued operations in 2008 was \$1.0 million compared with \$1.3 million in 2007.

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Cash used in investing activities in 2008 was \$338.4 million, compared to \$8.0 million in 2007, a difference of \$330.4 million. The increase in cash used in investing activities was primarily attributable to the following factors:

Cash used to purchase Excel, net of cash acquired, was \$358.3 million in 2008. This compares to \$3.0 million used for our acquisition of the U.K. optics business in 2007;

We used \$18.0 million to purchase property and equipment in 2008, compared to \$4.6 million in 2007, the majority of which related to our newly leased Bedford, MA facility;

Proceeds from the sale of discontinued operations in 2008 was \$21.6 million, and there were no such proceeds in 2007;

Change in long term assets and liabilities of \$12.1 million in 2008, compared to \$0.1 million in 2007; and

We generated \$3.2 million in 2008 from the sale of property, plant, and equipment as a result of our restructuring efforts with the U.K. and China operations. There were no such proceeds in 2007.

Cash provided by investing activities of discontinued operations was \$1.0 million compared with a \$0.5 million of cash used in 2007.

Cash provided by financing activities in 2008 was \$196.9 million, compared to \$0.8 million in 2007, a difference of \$196.2 million. The increase was primarily attributable to the following factors:

In 2008, we received cash proceeds, net of issuance costs, of \$203.5 million from the issuance of our Senior Notes that were used to fund a portion of our acquisition of Excel. We did not issue any debt in 2007;

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In 2008, we received \$0.1 million primarily from the exercise of stock options, whereas in 2007 we received approximately \$8.2 million; and

The cash we used to repurchase shares was \$6.4 million in 2008, compared to \$7.8 million in 2007.

In addition to cash flows from operating, investing and financing activities, exchange rate changes resulted in a decrease of \$0.8 million in our cash balances, compared to an increase of \$3.7 million in 2007.

*Cash Flows for the Year Ended December 31, 2007 and December 31, 2006*

Cash provided by operations in 2007, was \$37.6 million, compared to \$35.2 million in 2006, a difference of \$2.4 million, or 6.8%. The increase was primarily attributable to the following factors:

In 2007, we recorded net income of \$15.2 million, compared to net income of \$7.5 million in 2006;

Other non-cash charges, such as depreciation and amortization of fixed assets and intangible assets, non-cash related restructuring charges, and share based compensation were \$20.3 million in 2007 and \$13.9 million in 2006. The increase in 2007 was primarily composed of \$3.4 million in non-cash restructuring charges that did not exist in 2006, and a \$2.5 million share based compensation charge in 2007 compared with a \$0.7 million charge in 2006;

A \$20.2 million increase in our accounts receivable balances in 2007, as compared to \$1.5 million decrease in 2006;

Inventory balances in 2007 provided cash of \$5.4 million, as compared to using \$5.0 million of cash in 2006; and

The net change in deferred revenue and the related deferred cost of goods sold provided \$7.3 million in 2007, and in 2006 those same accounts provided \$19.6 million in cash; and in 2007, the net cash flows generated from accounts payable and accrued expenses were \$4.1 million, as compared to cash flow used from these activities of \$12.0 million in 2007.

Cash used in the operations of discontinued operations was \$1.3 million in 2007 compared with an immaterial cash flow impact in 2006.

Cash used in investing activities in 2007 was \$8.0 million, compared to cash provided by investing activities of \$33.0 million in 2006, a difference of \$41.0 million. The change was primarily attributable to the following factors:

In 2006, we had a net sale of investments of \$26.7 million, and we sold property, plant and equipment for \$6.3 million. We had no such activity in 2007;

We used 4.6 million of cash to purchase property, plant and equipment in 2007, as compared to \$1.1 million of purchases in 2006; and

We used \$3.0 million in 2007 to purchase our U.K. optics business. No such purchases occurred in 2006.

Cash used in investing activities of discontinued operations was \$0.5 million and \$0.6 million in 2007 and 2006, respectively.

Cash provided by financing activities in 2007 was \$0.8 million, compared to \$2.1 million in 2006, a difference of \$1.3 million. The decrease was primarily attributable to the following factors:

Cash received from the exercise of stock options, which provided \$8.2 million in 2007 and \$4.9 million in 2006; and

Cash we used to repurchase our common shares, which was \$7.8 million in 2007 and \$3.8 million in 2006.

In addition to cash flows from operating, investing and financing activities, cash generated from exchange rate changes resulted in an increase of \$3.7 million in our cash balances compared to decreasing cash balances by \$1.2 million in 2006.

### **Other Liquidity Matters**

#### *Debt*

On August 20, 2008 (the Closing Date), we issued to various investors \$210.0 million of unsecured senior notes (the Senior Notes), along with detachable warrants (the Warrants) for the purchase of 5,882,520 of our common shares, for collective net proceeds to us of \$203.5 million. The proceeds were used to fund a portion of our acquisition of Excel. The Senior Notes carry a fixed interest rate of 11.0%. The Warrants were net exercised by the holders in October 2008, in exchange for 5,858,495 of our common shares. We ascribed a fair value to the Warrants in the amount of \$26.3 million as of the Closing Date. The fair value was based upon the Black-Scholes option pricing model, assuming a risk-free interest rate of 3.0%, an expected term of 5.0 years, a volatility rate of 85.0% and no dividends.

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The Senior Notes pay interest semi-annually and mature in August 2013. After the first year anniversary of the Closing Date, we may redeem up to 50% of the Senior Notes with no penalty or premium. After the third anniversary of the Closing Date, we may redeem all remaining Senior Notes, again with no penalty or premium. The Senior Notes require us to comply with certain covenants that restrict the Company from taking on additional debt, repurchasing equity, making investments or selling certain assets. Under the Bankruptcy Code, our status as a bankruptcy debtor automatically accelerates the payment of all of our debt, including that arising under the Senior Notes. Accordingly, we have classified this debt as current in our December 31, 2008 consolidated financial statements. As further discussed above under *The Third Modified Joint Chapter 11 Plan of Reorganization* the holders of the Senior Notes have agreed to exchange their Senior Note Claims in exchange for: (i) approximately 53.8% of GSIG's post-consummation outstanding shares, (ii) new secured notes in the aggregate amount of \$110 million, (iii) excess cash available under the Plan to the extent certain allowed claims exceed \$22.5 million, and (iv) their pro rata portion of the Cash Payment.

The \$26.3 million value of the Warrants was recorded as a discount against the debt. This discount is being amortized to interest expense using the effective interest method over the life of the Senior Notes. In connection with the issuance of the Senior Notes, we incurred \$6.5 million in issuance fees, which have been capitalized as debt issuance costs, and are included in other current assets. These issuance fees are being amortized to interest expense on the effective interest method over the contractual term of the Senior Notes. As of December 31, 2008, the unamortized portion of the valuation of the Warrants was \$24.9 million, and the unamortized debt issuance costs were \$6.0 million. The Senior Notes, net of the value of the Warrants and net of the debt issuance costs, constitute a net carrying value of \$185.1 million at December 31, 2008. There was no debt outstanding as of December 31, 2007. For the year ended December 31, 2008, the total amount recorded to interest expense, including the accretion of the Warrant value, and of the debt issuance costs, was \$10.2 million.

As discussed further at Note 2 of Notes to Consolidated Financial Statements, in connection with the Revenue Review, we failed to timely file our annual and quarterly reports. In connection with the issuance of the Warrants, the Company and the Warrant holders entered into a Registration Rights Agreement (the *RRA*), dated as of August 20, 2008, pursuant to which we agreed to register the common shares issuable upon exercise of the Warrants. We filed that registration statement on Form S-3 in October 2008, simultaneously with the exercise of the Warrants. As a result of our failure to file our Quarterly Report on Form 10-Q for the period ended September 26, 2008, on November 12, 2008 we notified the former Warrant holders that we were indefinitely suspending the Company's registration statement on Form S-3. Pursuant to the *RRA*, the Company is obligated to maintain the effectiveness of the registration statement until the earlier of (i) the date which is twelve (12) months after the Effective Time (October 23, 2008) and (ii) the date on which there are no registrable securities (the *Maintenance Period*). Under the *RRA*, monetary penalties accrue and are payable to the former Warrant holders for failure to maintain an effective registration statement during the *Maintenance Period*, subject to certain terms and conditions more specifically set forth therein. In 2008, we incurred penalties under the *RRA* and have accordingly recorded expenses and corresponding accrued liability of \$0.8 million in 2008. We have continued to incur penalties under the *RRA* into 2009. The maximum penalty payments payable under these provisions is approximately \$4.0 million.

As disclosed above, on November 20, 2009, the Debtors filed for voluntary petitions for relief under Chapter 11 of the Bankruptcy Code of the Bankruptcy Court. For additional information regarding our liquidity and capital resources see Item 7, *Management's Discussions and Analysis of Financial Condition and Results of Operation Overview Chapter 11 Bankruptcy Filings*.

*Pension Plans*

We maintain two plans that are considered to be defined benefit plans under the provisions of SFAS 158, a plan in the U.K., and a plan in Japan. As of December 31, 2008, based on the provisions of SFAS 158, the value of the U.K. Plan's assets was \$18.0 million, and the projected benefit obligations were \$20.8 million, resulting in a liability of \$2.8 million. The Japan pension plan has assets of \$0.8 million, and a projected benefit obligation of \$2.1 million, resulting in a liability of \$1.3 million at December 31, 2008.

Our funding policy is to fund pensions and other benefits based on actuarial methods as permitted by regulatory authorities. The results of funding valuations depend on the assumptions that we make with regard to attributes such as asset returns, rates of members' benefits increases, mortality, retail price inflation and other market driven changes. The assumptions used represent one estimate of a possible future outcome. The final cost to us will be determined by events as they actually become known. Because of the underfunded positions that our pension plans currently have and potential changes in the actual outcomes relative to our assumptions, we may have to increase payments to fund these plans in the future.

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In the U.K., funding valuations are conducted every three years, based on the last completed funding valuation on November 30, 2006, the Company and the Plan Trustees agree to a schedule of contributions under which the Company is contributing approximately \$48,000 per month until March 2018. We have since changed our U.K. plan year end to December 31, and so we are required to conduct a funding valuation sooner than the previously scheduled date of November 30, 2009. Accordingly, we have begun a funding valuation as of December 31, 2008. Upon the completion of this valuation, these monthly contributions may change. The Japanese plan includes a guarantee of return of principal and yearly interest 0.75%; therefore, there are no significant fluctuations in this plan.

See Note 11 of Notes to Consolidated Financial Statements for further information about these plans.

**Off-Balance Sheet Arrangements, Contractual Obligations***Contractual Obligations*

The following table summarizes our contractual obligations at December 31, 2008 and the effect such obligations are expected to have on liquidity and cash flow in future years. The Company has excluded the future cash payments for FIN 48 tax liabilities because the timing of the settlement of these liabilities can not be estimated by year. However, these FIN 48 liabilities have been classified as long-term on the consolidated balance sheets.

Our contractual obligations may be affected by the filing of voluntary petitions for relief under Chapter 11 of the Bankruptcy Code by the Debtors and therefore may not be paid in full, or in accordance with the original contractual terms, as a result.

Contractual Obligations	Total	2009	2010-2011	2012-2013	Thereafter
	(In thousands)				
11.0% Unsecured Senior Notes (1)	\$ 210,000	\$ 210,000	\$	\$	\$
Interest on 11.0% Unsecured Senior Notes (2)	106,838	23,100	46,200	37,538	
Penalty relating to warrants (3)	4,040		4,040		
Operating leases (4)	28,993	5,440	8,985	5,159	9,409
Purchase commitments (5)	11,235	9,178	2,036	21	
Deferred compensation (5)	702	702			
U.K. pension plan (6)	5,328	576	1,152	1,152	2,448
Total contractual cash obligations	\$ 367,136	\$ 248,996	\$ 62,413	\$ 43,870	\$ 11,857

- (1) The \$210 million of 11% Unsecured Senior Notes are outstanding as of the date of this report and represent a contractual obligation of the Company. The 11% Unsecured Senior Notes are not shown as a contractual obligation after 2009 due to the voluntary petition filed by GSI Group, Inc and two of its United States subsidiaries for relief under chapter 11 of the United States Bankruptcy Code. See Note 8 of Notes to Consolidated Financial Statements and Significant Recent Events Chapter 11 Bankruptcy Filing in Item 1, *Business* of this Annual Report on Form 10-K for additional information.
- (2) Interest on the 11% Unsecured Senior Notes is shown through the currently scheduled maturity date in 2013. The actual amount of interest paid in 2010 through 2013 may be different from the amounts shown in the table depending on the outcome of the Chapter 11 bankruptcy proceedings. Interest is due and payable semi-annually.
- (3) Estimated penalties incurred as a result of our inability to maintain the effectiveness of our registration statement on Form S-3, filed in October 2008, relating to the resale of our common shares issued upon the exercise of the Warrants. See Note 14 of Notes to Consolidated Financial Statements.
- (4) These amounts represent the gross payments payable for facilities that we lease. These amounts do not reflect anticipated sub-lease income of approximately \$0.7 million, in total, from 2009 to 2013. See Note 14 of Notes to Consolidated Financial Statements.
- (5) See Note 14 of Notes to Consolidated Financial Statements.
- (6) Represents the contractual obligation of payments equivalent to \$48,000 per month through March 2018.

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### *Off-Balance Sheet Arrangements*

Through December 31, 2008, we have not entered into any off-balance sheet arrangements or material transactions with unconsolidated entities or other persons.

### **Critical Accounting Policies and Estimates**

The preparation of financial statements in conformity with generally accepted accounting principles requires us 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, we evaluate our estimates, assumptions and judgments, including those related to revenue recognition, fair value measurements, allowance for doubtful accounts, inventory costing and reserves, the assessment of the valuation of goodwill, intangible assets and tangible long-lived assets, accounting for business combinations, 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 our estimates.

We believe that the following critical accounting policies most significantly affect the portrayal of our financial condition and results of operations and require the most difficult and subjective judgments.

**Revenue Recognition.** We recognize 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.

We follow the provisions of Emerging Issues Task Force ( EITF ) 00-21, Revenue Arrangements with Multiple Deliverables for all multiple element arrangements. Under EITF 00-21, we assess whether the deliverables 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. We apply 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, we recognize 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 unit of each product has been delivered.

Although certain of our products contain operating and application software, we have determined the software element is incidental in accordance with the AICPA's Statement of Position ( SOP 97-2 ) and EITF 03-05, Applicability of AICPA Statement of Position 97-2 to Non-Software Deliverables in an Arrangement Containing More-Than-Incidental Software.

We determine the unit of accounting for certain transactions based on the guidance in TPA 5100.39. In particular, 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. We generally design, market and sell these products as standard configurations. For those standard configurations where acceptance criteria, if any, exist and are demonstrated prior to shipment, revenue is recorded at the time of shipment. For those cases where acceptance criteria cannot be demonstrated prior to shipment of a product or if a significant amount of fees are due upon acceptance, we recognize revenue upon customer acceptance. Acceptance is generally required for sales of Semiconductor Systems Segment products to Japanese customers, sales of New Products, which are considered by us, 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. We follow 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.

Precision Technology Segment and Excel Segment transactions include 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. Revenue is generally recognized under the multiple units shipped methodology described above.





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Our Semiconductor Systems Segment also sells spare parts and consumable items, which are not subject to acceptance criteria. Revenue for these spare parts and consumable items is generally recognized under the multiple units shipped methodology described above.

Installation is generally a routine process that occurs within a short period of time from delivery and we have 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 SFAS 5, Accounting for Contingencies, as we have 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. Our estimate of costs to service the warranty obligations are based on historical experience and expectations of future conditions. To the extent we experience 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.

We also sell optional extended warranty services, and preventative maintenance contracts, at the time of their product purchase. We account for these agreements in accordance with provisions of FASB Technical Bulletin (FTB) 90-1 Accounting for Separately Priced Extended Warranty and Product Maintenance Contracts under which we recognize the separately priced extended warranty and preventative maintenance fees over the associated period.

We, at the request of our customers, may at times perform professional services for our 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 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.

We typically negotiate trade discounts and agreed terms in advance of order acceptance and record any such items as a reduction of revenue. Our 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 our review of customer creditworthiness and other factors, we may provide our customers with payment terms that exceed 180 days. To the extent all other revenue recognition criteria have been met, we recognize revenue for these extended payment arrangements as the payments become due.

We have significant deferred revenue included in our accompanying consolidated balance sheets, with balances (including both current and long-term amounts) of \$84.2 million and \$101.6 million as of December 31, 2008 and 2007, respectively. A significant majority of these amounts relate to arrangements whereby the entire arrangement has been accounted for as deferred revenue, as there is no fair value for the undelivered elements. Upon the final delivery of the undelivered element(s) of the arrangement, the revenue will be recorded for that arrangement. To a lesser extent, the deferred revenue balances relate to either: (a) the unrecognized portion of a multiple element arrangements that is being recognized into revenue over a ratable basis as associated services are performed; (b) arrangements not currently recognizable due to the arrangement not being fixed and determinable at its inception; (c) the future amortization to revenue of extended warranty contracts and preventative maintenance plans; (d) revenue deferrals for product shipments with FOB destination shipping terms; and (e) deposits from customers against future orders. The classification of deferred revenue, and deferred cost of goods sold, is based on our expectations relative to when the revenue will be recognized, based on facts known to us as of the date our financial statements are released.

**Fair Value Measurements.** On January 1, 2008, we adopted SFAS 157, Fair Value Measurements, with no impact on our consolidated results and financial position. SFAS 157 defines fair value, establishes a framework for measuring fair value, and enhances 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. SFAS 157 establishes a value hierarchy based on three levels of inputs, of which the first two are considered observable and the third is considered unobservable.

Included in our financial assets with fair value measurements are \$32.3 million in par value auction rate securities that we acquired in connection with our purchase of Excel. These auction rate securities are level 3 assets for which no observable market value exists, and for which we have valued based on assumptions the market participants might use in their estimates of fair value. As of December 31, 2008, the auction rate securities have a fair value of \$25.1 million.



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Included in our financial liabilities with fair value measurements are \$210.0 million of Senior Notes. These senior notes have a fair value of \$145.0 million, based on quoted prices for similar liabilities, or similar liabilities traded as assets.

**Allowances for Doubtful Accounts.** We are required to estimate the collectability of our trade receivables. A considerable amount of judgment is required in assessing the ultimate realization of receivables, including the current credit-worthiness of each customer. We maintain an allowance for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. If the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required. The collectability of accounts receivable is evaluated based on a combination of factors. In circumstances where we are aware of a specific customer's inability to meet its financial obligations (e.g., bankruptcy filings), a specific reserve for bad debts is recorded against amounts due, to reduce the net recognized receivable to the amount we reasonably believe will be collected. For all other customers, we estimate an allowance for bad debts based upon the total accounts receivable balance and the percentage expected to be realized through subsequent cash collections. If circumstances change (i.e., higher than expected defaults or an unexpected material adverse change in a major customer's ability to meet its financial obligations to us), our estimates of the recoverability of amounts due to us could be reduced by a material amount.

**Inventories.** Inventories are stated at the lower of cost or market, after provisions for excess and obsolete inventory salable at prices below cost. Costs are determined using first-in, first-out method.

We write down inventory for estimated obsolescence or unmarketable inventory equal to the difference between the cost of inventory and the estimated market value based upon assumptions about future demand and market conditions. If actual market conditions are less favorable than those projected by us, additional inventory write-downs may be required.

**Business Combinations.** In accordance with SFAS 141, Business Combinations, we allocate the purchase price of acquired companies to the tangible and intangible assets acquired and liabilities assumed as well as to in-process research and development based upon their estimated fair values at the acquisition date. The purchase price allocation process requires management to make significant estimates and assumptions, especially at acquisition date with respect to intangible assets, support obligations assumed, estimated restructuring liabilities and pre-acquisition contingencies.

Although we believe the assumptions and estimates we have made in the past have been reasonable and appropriate, they are based in part on historical experience and information obtained from the management of the acquired companies and are inherently uncertain. Examples of critical estimates in valuing certain of the intangible assets we have acquired or may acquire in the future include but are not limited to:

future expected cash flows from sales of acquired product lines, developed technologies and patents;

expected costs to develop in-process research and development projects into commercially viable products and the estimated cash flows from the projects when completed;

the acquired company's brand and competitive position, as well as assumptions about the period of time the acquired brand will continue to be used in the combined company's product portfolio; and

discount rates.

Unanticipated events and circumstances may occur which may affect the accuracy or validity of such assumptions, estimates or actual results.

Effective January 1, 2009, we adopted SFAS 141 (revised 2007), Business Combinations. Refer to Recent Accounting Pronouncements below for additional information.

**Goodwill, Intangible Assets and Impairment Assessment.** As discussed above, in Business Combinations, our goodwill and intangible assets generally arise from business combinations. Our most significant intangible assets are acquired technology, customer relationships, and trademarks and trade names. The purchase price we pay for acquired companies is allocated first to the acquired tangible assets and liabilities at their fair value. Any excess purchase price is then allocated to identifiable intangible assets and the remainder, if any, is assigned to goodwill. We make various assumptions and estimates in order to assign fair value to acquired tangible and intangible assets and liabilities, including those

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associated with our business plans and related cash flow forecasts, as well as discount rates and terminal values, among others. Actual cash flows may vary from forecasts used to value the intangible assets at the time of the business combination.

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Our most significant intangible assets are acquired technology, customer relationships, and trademarks and trade names. In addition to our review of the carrying values of each asset, the useful life assumptions for each asset, including the classification of certain intangible assets as indefinite lived, are reviewed on a periodic basis to determine if changes in circumstances warrant revisions to them. All definite-lived intangible assets are amortized over the periods in which their economic benefits are expected to be realized.

We test our goodwill for impairment on an annual basis in accordance with SFAS 142, Goodwill and Other Intangible Assets, which first requires a comparison of the carrying value of each of our reporting units' net assets to their fair value. If the carrying value of a reporting unit exceeds its fair value, we calculate the implied fair value of the reporting unit's goodwill and compare it to the goodwill's carrying value. If the carrying value of goodwill exceeds its implied fair value, an impairment charge is recorded for the difference. The implied fair value of goodwill is calculated by performing a fair value assessment of the assets and liabilities of the reporting unit, in a manner consistent with the discussion above with respect to the initial fair value allocation performed in a business combination. The carrying value of each reporting unit's assets and liabilities are predominantly specifically identifiable. Additionally, reporting units that benefit from corporate assets or liabilities are allocated a portion of those corporate assets and liabilities on a systematic, proportional basis.

Our indefinite-lived intangible assets represent trade names that were acquired in the August 2008 Excel acquisition. The Company will assess these indefinite-lived intangible assets for impairment on an annual basis and periodically reassess their continuing classification as indefinite-lived. Discounted cash flow forecasts for each indefinite-lived intangible asset are used to fair value them. Impairment exists if the fair value of the intangible asset is less than its carrying value. An impairment charge equal to the difference is recorded to reduce the carrying value to its fair value.

We evaluate amortizable intangible assets and other long-lived assets for impairment, in accordance with SFAS 144, Accounting for the Impairment or Disposal of Long-lived Assets, whenever changes in events or circumstances indicate carrying values may exceed their undiscounted cash flow forecasts. If undiscounted cash flow forecasts indicate the carrying value of a definite-lived intangible asset may not be recoverable, a fair value assessment is performed. Fair value estimates are derived from discounted cash flow forecasts for the intangible asset. If fair value is less than carrying value, an impairment charge equal to the difference is recorded, thereby reducing the intangible asset's carrying value to its fair value. We also review the useful life assumptions for definite-lived intangible assets on a periodic basis to determine if changes in circumstances warrant revisions to them. All definite-lived intangible assets are amortized over the periods in which their economic benefits are expected to be realized.

Factors which may trigger an impairment of our goodwill, intangible assets and other long-lived assets include the following:

underperformance relative to historical or projected future operating results;

changes in the manner of our use of acquired assets or the strategy for our overall business;

negative industry or economic trends;

interest rate changes;

technological changes or developments;

changes in competition;

loss of key customers or personnel;

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adverse judicial or legislative outcomes or political developments;

declines in our stock price for a sustained period; and

the decline of our market capitalization below net book value.

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The occurrence of any of these events or any other unforeseeable event or circumstance that materially affects future results or cash flows may cause an impairment that is material to our results of operations or financial position in the reporting period in which it occurs or is identified.

The significant downturn in the global economy experienced in 2008, and most notably in the fourth quarter of 2008, negatively impacted our estimated future revenues and cash flows, as compared to our prior estimates, including those estimates made at the time we acquired Excel. Excel's 2009 unaudited actual revenues were approximately 32% lower than Excel's 2009 projected revenues at the time of the acquisition in August 2008. From the acquisition in August 2008 to December 2008, when the impairment analysis was performed, we reduced Excel's annual revenue projections by \$50.1 to \$54.5 million per year, or on average approximately 26% per year, compared to the projections used to initially value the intangible assets in Excel's purchase price allocation. During this same period of time, the Company's cost of capital increased significantly, primarily due to the increase in risk associated with an investment in the Company's equity securities. Our estimated cost of capital increased in the fourth quarter of 2008 after we announced the delayed filing of our financial results, as further discussed in Note 2 of the Company's Notes to Consolidated Financial Statements. The announcement increased our risk profile and made financing more expensive, as a result of the decline in the Company's stock price, the receipt by the Company of default notices from its noteholders, and the severe economic downturn. Our weighted average cost of capital forms the basis of the rates used to discount our cash flow forecasts which are integral to our fair value estimates. The discount rates utilized to initially value the intangible assets in the purchase price allocation ranged from 10.0% to 13.0%, while the discount rates utilized in the December 31, 2008 impairment analyses of the goodwill and other intangible assets ranged from 16.5% to 17.5%. Consequently, we undertook an impairment review of our goodwill, intangible assets and other long-lived assets (property, plant and equipment) as of December 31, 2008. This review led to us recording a charge to reduce the carrying value of these assets by an aggregate of \$215.1 million. The results of the impairment review are summarized in the following table (in thousands):

	Pre-impairment Net Carrying Value	Impairment Charge	Post-impairment Net Carrying Value
Goodwill	\$ 176,232	\$ (131,169)	\$ 45,063
Indefinite-lived intangible assets	34,341	(21,314)	13,027
Definite-lived intangible assets	115,563	(57,130)	58,433
Property, plant and equipment	59,877	(5,438)	54,439
	\$ 386,013	\$ (215,051)	\$ 170,962

No impairment charges were recorded in 2007 or 2006. Following our 2008 impairment charge, we continue to maintain a significant balance in our goodwill, intangible assets and other long-lived assets. The following table shows the December 31, 2008 breakdown of goodwill, intangibles and property, plant and equipment by reportable segment:

	Goodwill	Intangible Assets	Property, Plant & Equipment
Precision Technology	\$ 9,245	\$ 10,460	\$ 7,816
Semiconductor Systems			1,236
Excel	35,818	61,000	30,273
Corporate			15,114
	\$ 45,063	\$ 71,460	\$ 54,439

To the extent that our assumptions used to value the assets as of December 31, 2008 should adversely change or there is a further deterioration of the markets we serve, the broader worldwide economy, or the performance of our business relative to our expectations as of December 31, 2008, we may be required to record additional impairment charges in the future.

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**Restructuring and Other Charges.** In accounting for our restructuring activities, we follow the provisions of SFAS 146, Accounting for Costs Associated with Exit or Disposal Activities. In accounting for these obligations, we make assumptions related to the amounts of employee severance, benefits, and related costs and to the time period over which facilities will remain vacant, sublease terms, sublease rates and discount rates. Estimates and assumptions are based on the best information available at the time the obligation has arisen. These estimates are reviewed and revised as facts and circumstances dictate; changes in these estimates could have a material effect on the amount previously expensed against our earnings, and currently accrued on our consolidated balance sheet. The costs incurred to third parties, including attorneys, forensic accountants, and other advisors that related to the Company's Revenue Review have been included in the Company's 2008 restructuring and other charges. These costs are charged to expense as incurred.

**Pension Plans.** Two of our subsidiaries, located in the United Kingdom and Japan, maintain retirement plans that are accounted for as defined benefit plans. In 2006, the Company implemented accounting statement SFAS 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans. The impact of the adoption of the measurement date provision of SFAS 158 was not material.

Our United Kingdom pension plan was closed to new membership in 1997 and we curtailed our sponsorship in 2002, limiting our obligation to benefits earned through that date. Benefits under this plan were based on the employees' years of service and compensation. We continue to follow our policy to fund this pension plan based on widely accepted actuarial methods. At December 31, 2008, the market value of the plan assets was \$2.8 million less than the projected benefit obligation.

The accounting rules applicable to our United Kingdom pension plan require amounts recognized in financial statements be determined on an actuarial basis, rather than as contributions are made to the plan. Since the market value of our pension assets is less than the accumulated pension benefit obligation, we recorded a \$0.7 million non-cash charge to other comprehensive income in stockholders' equity and an accrued long-term pension liability in 2008. At December 31, 2008, the cumulative balance of this non-cash charge amounted to \$2.8 million. These charges to equity did not affect our net income. In 2008, we funded \$0.6 million to the plan.

Our Japanese pension plan is a tax qualified plan that covers substantially all Japanese employees. Benefits are based on years of service and the employee's compensation at retirement. We fund the plan sufficient to meet current benefits as well as fund a certain portion of future benefits as permitted in accordance with regulatory authorities. Since this is an active plan, a significant portion of the pension benefit obligation is determined based on the rate of future compensation increases. We deposit funds under various fiduciary-type arrangements and/or purchase annuities under group insurance contracts. At December 31, 2008, the market value of the plan assets was \$1.3 million less than the projected benefit obligation.

Given both pension plans' current under-funded status, changes in economic and market conditions may require us to increase cash contributions in future years.

**Accounting for Income Taxes.** As part of the process of preparing its consolidated financial statements, the Company is required to estimate its income tax provision (benefit) in each of the jurisdictions in which the Company operates. This process involves estimating its current income tax provision (benefit) together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within its consolidated balance sheet.

The Company records a valuation allowance to reduce its deferred tax assets to an amount that more likely than not will be realized. While the Company has considered future taxable income and ongoing prudent and feasible tax planning strategies in assessing the need for the valuation allowance, in the event the Company determines that it will be able to realize its deferred tax assets in the future in excess of its net recorded amount, a reduction to the valuation allowance for the deferred tax assets would increase income in the period such determination was made. Likewise, should the Company determine that it would not be able to realize all or part of its net deferred tax assets in the future, an adjustment to the valuation allowance for the deferred tax assets would decrease income in the period such determination was made.

The amount of income taxes the Company pays is subject to ongoing audits by federal, state and foreign tax authorities, which often results in proposed assessments. Its estimate for the potential outcome for any uncertain tax issue is highly judgmental. The Company believes that it has adequately provided for any reasonably foreseeable outcome related to these matters. However, its future results may include favorable or unfavorable adjustments to its estimated tax liabilities in the period that the assessments are made or resolved, or when the statute of limitations for certain periods expires. As a result, its effective tax rate may fluctuate significantly on a quarterly basis.



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Undistributed earnings of the Company's non Canadian subsidiaries amounted to approximately \$81.0 million as of December 31, 2008. The Company has not provided any additional federal or state income taxes or foreign withholding taxes on the undistributed earnings as such earnings have been indefinitely reinvested in the business as defined in the provisions of SFAS 109 as well as Accounting Principles Board ( APB ) 23. The determination of the amount of the unrecognized deferred tax liability related to the undistributed earnings is not practicable because of the complexities associated with its hypothetical calculation.

Effective January 1, 2007, the Company adopted FASB Interpretation ( FIN ) 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109. FIN 48 prescribes a recognition threshold and a measurement attribute for the financial statement recognition and measurement of tax positions taken or expected to be taken in a tax return. For those benefits to be recognized, a tax position must be more likely than not to be sustained upon examination by taxing authorities.

The Company assessed all material positions taken in any income tax return, including all significant uncertain positions, in all tax years that are still subject to assessment or challenge by relevant taxing authorities. Assessing an uncertain tax position begins with the initial determination of the position's sustainability and is measured at the largest amount of benefit that is greater than 50 percent likely of being realized upon ultimate settlement. As of each balance sheet date, unresolved uncertain tax positions must be reassessed, and the Company will determine whether (i) the factors underlying the sustainability assertion have changed and (ii) the amount of recognized tax benefit is still appropriate. The recognition and measurement of tax benefits requires significant judgment. Judgments concerning the recognition and measurement of a tax benefit might change as new information becomes available.

**Loss Contingencies.** We are subject to legal proceedings, lawsuits and other claims relating to labor, service and other matters arising in the ordinary course of business. Quarterly, we review the status of each significant matter and assess our potential financial exposure. If the potential loss from any claim or legal proceeding is considered probable and the amount can be reasonably estimated, we accrue a liability for the estimated loss. Significant judgment is required in both the determination of probability and the determination as to whether an exposure is reasonably estimable. Because of uncertainties related to these matters, accruals are based only on the best information available at the time. As additional information becomes available, we reassess the potential liability related to our pending claims and litigation and may revise our estimates. Such revisions in the estimates of the potential liabilities could have a material impact on our results of operations and financial position.

***Recent Accounting Pronouncements***

See Note 3 of Notes to Consolidated Financial Statements for recent accounting pronouncements that could have an effect on us.

**Item 7A. Quantitative and Qualitative Disclosures about Market Risk**

We are exposed to market risk from changes in foreign currency exchange rates and interest rates, which could affect operating results, financial position and cash flows. We manage our exposure to these market risks through our regular operating and financing activities and, when appropriate, through the use of derivative financial instruments.

***Foreign Currency Exchange Rate Risk and Sensitivity***

We are exposed to changes in foreign currency exchange rates. Any foreign currency transaction, defined as a transaction denominated in a currency other than the U.S. dollar, will be reported in U.S. dollars at the applicable exchange rate. Assets and liabilities are translated into U.S. dollars at exchange rates in effect at the balance sheet date and income and expense items are translated at average rates for the period. The primary foreign currency denominated transactions include revenue and expenses and the resulting accounts receivable and accounts payable balances reflected on our balance sheet. Therefore, the change in the value of the U.S. dollar compared to foreign currencies will have either a positive or negative effect on our financial position and results of operations. Historically, our primary exposure has related to transactions denominated in the Japanese Yen, Euro, British Pound and Canadian Dollar.

A hypothetical change of 10% in appreciation or depreciation in foreign currency exchange rates from the quoted foreign currency exchange rates at December 31, 2008 would not have a material impact on our revenue, operating results or cash flows.

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Periodically, we enter into forward exchange contracts to hedge against foreign currency fluctuations. The Company's primary objective for holding derivative financial instruments is to manage currency risk. In accordance with SFAS 133, Accounting for Derivative Instruments and Hedging Activities, the Company's accounting policies for these instruments are based on whether they meet the criteria for designation as hedging transactions, including cash flow, or net investment hedges.

The Company did not have any derivative instruments that qualify for hedge accounting under SFAS 133, Accounting for Derivative Instruments and Hedging Activities at December 31, 2008 or 2007. The Company records all derivatives at fair value as assets or liabilities in the consolidated balance sheet and any changes are recognized in other income and expense.

When the Company enters into foreign currency derivative contracts, the contracts are generally for less than six months duration with the purpose of hedging foreign currency risk on sales transactions. At December 31, 2008, the Company held no derivative contracts. At December 31, 2007, the Company held forward contracts to: sell Japanese yen for the equivalent of \$7.9 million; settle U.S. dollar / Japanese yen average strike option with an underlying currency amount of 400 million Japanese yen (equivalent \$3.5 million); and buy British pound for the equivalent of \$4.2 million.

***Interest Rate Risk and Sensitivity***

The Company's exposure to market risk associated with changes in interest rates relates primarily to its cash and cash equivalents, short-term investments, long-term investments and debt obligations. At December 31, 2008, the Company had \$69.0 million invested in cash and cash equivalents, as compared to \$172.4 million at December 31, 2007. Due to the average maturities and the nature of the cash portfolio at December 31, 2008, a one percent change in interest rates could have a \$0.7 million impact on interest income on an annual basis. The Company does not actively trade derivative financial instruments, but may use them to manage interest rate positions associated with its debt instruments. The Company did not hold interest rate derivative contracts as of December 31, 2008.

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**Item 8. Financial Statements and Supplementary Data**

**GSI GROUP INC.**

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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and Shareholders of GSI Group Inc.

We have audited the accompanying consolidated balance sheets of GSI Group Inc. as of December 31, 2008 and 2007, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2008. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of GSI Group Inc. at December 31, 2008 and 2007, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2008, in conformity with U.S. generally accepted accounting principles.

As discussed in Note 2 to the consolidated financial statements, the Company has restated its financial statements for the years ended December 31, 2007 and 2006 to correct certain errors in the area of revenue recognition and the effects on other accounts.

The accompanying financial statements have been prepared assuming that GSI Group Inc. will continue as a going concern. As more fully described in Note 1 to the consolidated financial statements, on November 20, 2009, the Company voluntarily filed petitions on behalf of the Parent and two subsidiaries for relief under Chapter 11 of the United States Bankruptcy Code. This filing caused the Company to be in default with covenants under its loan agreement. These conditions raise substantial doubt about the Company's ability to continue as a going concern, given the uncertainty with respect to the realization of the value of its assets, and its ability to discharge its liabilities. Management's plans in regard to these matters also are described in Note 1. The 2008 consolidated financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classification of liabilities that may result from the outcome of this uncertainty.

We have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), GSI Group Inc.'s internal control over financial reporting as of December 31, 2008, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated April 13, 2010 expressed an adverse opinion thereon.

/s/ ERNST & YOUNG LLP

Boston, Massachusetts  
April 13, 2010

**Table of Contents****GSI GROUP INC.****CONSOLIDATED BALANCE SHEETS****(In thousands of U.S. dollars, except share data)**

	December 31, 2008	December 31, 2007 (As Restated)
<b>ASSETS</b>		
Current Assets		
Cash and cash equivalents	\$ 69,001	\$ 172,387
Accounts receivable, net of \$1,687 and \$374, respectively	50,494	71,631
Income taxes receivable	30,038	21,790
Inventories	78,508	64,139
Deferred tax assets	11,106	8,541
Deferred cost of goods sold	20,507	37,194
Deferred debt financing costs	5,999	
Other current assets	9,569	7,120
Current assets of discontinued business held for sale		3,864
Total current assets	275,222	386,666
Property, plant and equipment, net of accumulated depreciation and amortization	54,439	28,382
Deferred tax assets	23,802	16,589
Deferred cost of goods sold	23,133	12,758
Investments in auction rate securities	25,065	
Other assets	2,133	1,566
Intangible assets, net	71,460	29,775
Goodwill	45,063	26,291
Noncurrent assets of discontinued business held for sale		5,618
Total assets	\$ 520,317	\$ 507,645
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current Liabilities		
Debt (Note 8)	\$ 185,115	\$
Accounts payable	20,286	17,905
Income taxes payable		1,546
Accrued compensation and benefits	7,894	9,848
Deferred revenue	45,061	79,462
Deferred tax liabilities	486	286
Other accrued expenses	23,814	8,980
Current liabilities of discontinued business held for sale		1,577
Total current liabilities	282,656	119,604
Deferred revenue	39,164	22,101
Deferred tax liabilities	30,131	10,124
Accrued restructuring, net of current portion	1,072	1,015
Income taxes payable	5,166	3,966
Accrued pension liability	4,104	4,481
Other liabilities	5,127	676
Minority interest	220	
Total liabilities	367,640	161,967

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### Commitments and contingencies (Note 14)

#### Stockholders' equity:

Common shares, no par value; Authorized shares: unlimited; Issued and outstanding:

47,567,874 and 42,161,592, respectively	330,896	310,970
Additional paid-in capital	10,733	8,191
Retained earnings (accumulated deficit)	(184,716)	19,131
Accumulated other comprehensive income (loss)	(4,236)	7,386

Total stockholders' equity	152,677	345,678
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Total liabilities and stockholders' equity	\$	520,317	\$	507,645
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The accompanying notes are an integral part of these financial statements.

**Table of Contents****GSI GROUP INC.****CONSOLIDATED STATEMENTS OF OPERATIONS****(In thousands of U.S. dollars, except per share data)**

	Year Ended December 31,		
	2008	2007 (As Restated)	2006 (As Restated)
Sales	\$ 288,468	\$ 291,081	\$ 259,030
Cost of goods sold	190,850	177,948	156,632
<b>Gross profit</b>	<b>97,618</b>	<b>113,133</b>	<b>102,398</b>
Operating expenses:			
Research and development and engineering	33,449	29,861	30,130
Selling, general and administrative	65,904	59,545	62,893
Amortization of purchased intangible assets	5,714	2,213	2,131
Impairment of goodwill, intangible assets and other long-lived assets	215,051		
Restructuring and other	10,485	6,655	
Acquisition related in-process research and development charge	12,142		
<b>Total operating expenses</b>	<b>342,745</b>	<b>98,274</b>	<b>95,154</b>
Income (loss) from operations	(245,127)	14,859	7,244
Interest income	3,310	6,637	4,627
Interest expense	(10,388)	(128)	(597)
Foreign exchange transaction gains (losses)	928	589	(1,441)
Other income (expense), net	(604)	215	(63)
Income (loss) from continuing operations before income taxes	(251,881)	22,172	9,770
Income tax provision (benefit)	(39,032)	7,484	2,914
Income (loss) from continuing operations	(212,849)	14,688	6,856
Income from discontinued operations, net of tax	270	467	645
Gain on disposal of discontinued operations, net of tax	8,732		
<b>Net income (loss)</b>	<b>\$ (203,847)</b>	<b>\$ 15,155</b>	<b>\$ 7,501</b>
Net income (loss) from continuing operations per common share:			
Basic	\$ (4.94)	\$ 0.35	\$ 0.16
Diluted	\$ (4.94)	\$ 0.34	\$ 0.16
Net income from discontinued operations per common share:			
Basic	\$ 0.21	\$ 0.01	\$ 0.02
Diluted	\$ 0.21	\$ 0.01	\$ 0.02
Net income (loss) per common share:			
Basic	\$ (4.73)	\$ 0.36	\$ 0.18
Diluted	\$ (4.73)	\$ 0.35	\$ 0.18
Weighted average common shares outstanding - basic	43,125	42,364	41,896
Weighted average common shares outstanding - diluted	43,125	42,645	42,251

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





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## GSI GROUP INC.

## CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY

(In thousands of U.S. dollars)

	Capital Stock			Retained	Accumulated	Total	Comprehensive
	# Shares	Amount	Additional Paid-In-Capital	Earnings (Accumulated Deficit)	Other Comprehensive Income (Loss)		
<b>Balance, December 31, 2005 (As Originally Reported)</b>	41,628	\$ 309,545	\$ 3,339	\$ 7,688	\$ (14,016)	\$ 306,556	
Cumulative effect of restatement			264	(11,067)		(10,803)	
<b>Balance, December 31, 2005 (As Restated)</b>	41,628	309,545	3,603	(3,379)	(14,016)	295,753	
Net income				7,501		7,501	\$ 7,501
Exercise of stock options and warrants	643	4,863				4,863	
Repurchase of treasury shares	(381)	(3,773)				(3,773)	
Share based compensation			676			676	
Excess tax benefit of stock options			1,035			1,035	
Unrealized loss on investments, net of tax of \$0					(9)	(9)	(9)
Pension liability, net of tax of \$244					1,786	1,786	1,786
SFAS 158 Employer's Accounting for Defined Benefit Pension and Other Retirement Plans Transition Adjustment					(483)	(483)	
Foreign currency translation adjustments					10,327	10,327	10,327
<b>Balance, December 31, 2006 (As Restated)</b>	41,890	310,635	5,314	4,122	(2,395)	317,676	\$ 19,605
Net income				15,155		15,155	\$ 15,155
Exercise of stock options and warrants	955	8,179				8,179	
Issuance of restricted stock	134						
Repurchase of treasury shares	(817)	(7,844)				(7,844)	
Share based compensation			2,454			2,454	
Excess tax benefit of stock options			423			423	
Pension liability, net of tax of \$20					4,172	4,172	4,172
Cumulative effect of adoption of FIN48				(146)		(146)	
Foreign currency translation adjustments					5,609	5,609	5,609
<b>Balance, December 31, 2007 (As Restated)</b>	42,162	310,970	8,191	19,131	7,386	345,678	\$ 24,936
Net loss				(203,847)		(203,847)	\$ (203,847)
Exercise of stock options and warrants	5,875	26,365				26,365	

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Issuance of restricted stock	305							
Repurchase of treasury shares	(774)	(6,439)					(6,439)	
Share based compensation			2,761				2,761	
Excess tax expense of stock options and restricted stock			(219)				(219)	
Unrealized gain on investments, net of tax of \$0					80	80		80
Pension liability, net of tax of \$0					797	797		797
Foreign currency translation adjustments					(12,499)	(12,499)		(12,499)
<b>Balance, December 31, 2008</b>	<b>47,568</b>	<b>\$ 330,896</b>	<b>\$ 10,733</b>	<b>\$ (184,716)</b>	<b>\$ (4,236)</b>	<b>\$ 152,677</b>	<b>\$ (215,469)</b>	

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

**Table of Contents****GSI GROUP INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS**

(In thousands of U.S. dollars)

	2008	Year Ended December 31,	
		2007 (As Restated)	2006 (As Restated)
<b>Cash flows from operating activities:</b>			
Net income (loss)	\$ (203,847)	\$ 15,155	\$ 7,504
Adjustments to reconcile net income (loss) to net cash from operating activities:			
Income from operations of discontinued operations	(270)	(467)	(645)
Gain on disposal of discontinued operations	(8,732)		
Depreciation and amortization	18,906	14,463	13,256
Impairment of goodwill, intangible assets and property, plant and equipment	215,051		
Acquisition related in-process research and development charge	12,142		
Step-up value of acquired inventory sold	1,240		
Share based compensation	2,761	2,454	676
Deferred income taxes	(33,670)	1,057	7,357
Earnings from equity investments	56	(156)	
Unrealized (gain) loss on derivatives		102	(97)
Gain on disposal of property and assets	(1,208)		(187)
Non-cash interest expense	1,890		
Non-cash restructuring charges	3,563	3,401	
Changes in current assets and liabilities, net of effects from business acquired:			
Accounts receivable	37,759	(20,190)	1,480
Inventories	19,898	5,403	(4,980)
Deferred costs	5,724	(7,033)	(24,205)
Other current assets	(7,412)	6,380	3,224
Deferred revenue	(15,924)	14,297	43,770
Accounts payable, accruals and taxes receivable and payable	(8,020)	4,072	(11,952)
Cash used in operating activities of discontinued operations	(1,005)	(1,346)	(33)