DATA I/O CORP
Form 10-Q
August 12, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

**FORM 10-Q**

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

For the quarterly period ended **June 30, 2011**

or

( ) **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE**

**SECURITIES EXCHANGE ACT OF 1934**

For the transition period from _____ to _____

Commission file number: **0-10394**

**DATA I/O CORPORATION**

(Exact name of registrant as specified in its charter)

| Washington | 91-0864123 |
|---|---|
| (State or other jurisdiction of incorporation) | (I.R.S. Employer Identification No.) |

**6464 185th Ave NE, Suite 101, Redmond, Washington, 98052**
**(425) 881-6444**
(Address, including zip code, of registrant s principle executive offices and telephone number, including area code)

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

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

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

Large accelerated filer __ Accelerated filer __ Non-accelerated filer __ Smaller reporting company X

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

Shares of Common Stock, no par value, outstanding as of August 3, 2011:

9,270,560

**DATA I/O CORPORATION**

**FORM 10-Q**
**For the Quarter Ended June 30, 2011**

**INDEX**


| Part I. | | **Financial Information** | Page |
|---|---|---|---|
| | Item 1. | Financial Statements | 3 |
| | Item 2. | Management s Discussion and Analysis of Financial Condition and Results of Operations | 12 |
| | Item 3. | Quantitative and Qualitative Disclosures About Market Risk | 18 |
| | Item 4. | Controls and Procedures | 18 |
| Part II | | **Other Information** | |
| | Item 1. | Legal Proceedings | 19 |
| | Item 1A. | Risk Factors | 19 |
| | Item 2. | Unregistered Sales of Equity Securities and Use of Proceeds | 19 |
| | Item 3. | Defaults Upon Senior Securities | 19 |
| | Item 4. | [Removed and Reserved] | 19 |
| | Item 5. | Other Information | 19 |
| | Item 6. | Exhibits | 19 |
| Signatures | | | 21 |

**PART I - FINANCIAL INFORMATION**

**Item 1. Financial Statements**

**DATA I/O CORPORATION**
**CONSOLIDATED BALANCE SHEETS**
**(in thousands, except share data)**

| | | (unaudited) June 30, 2011 | | December 31, 2010 |
|---|---|---|---|---|
| **ASSETS** | | | | |
| CURRENT ASSETS: | | | | |
| Cash and cash equivalents | $ | 16,990 | $ | 18,942 |
| Trade accounts receivable, net of allowance for doubtful accounts of $135 and $138 | | 5,336 | | 4,975 |
| Inventories | | 3,926 | | 3,570 |
| Other current assets | | 475 | | 528 |
| TOTAL CURRENT ASSETS | | 26,727 | | 28,015 |
| Property, plant and equipment net | | 1,270 | | 1,256 |
| Intangible software technology net | | 3,014 | | - |
| Other assets | | 102 | | 153 |
| TOTAL ASSETS | $ | 31,113 | $ | 29,424 |
| **LIABILITIES AND STOCKHOLDERS EQUITY** | | | | |
| CURRENT LIABILITIES: | | | | |
| Accounts payable | $ | 917 | $ | 1,234 |
| Accrued compensation | | 1,155 | | 1,578 |
| Deferred revenue | | 1,413 | | 1,572 |
| Other accrued liabilities | | 800 | | 770 |
| Accrued costs of business restructuring | | - | | 58 |
| Income taxes payable | | 87 | | 108 |
| Current portion long-term debt | | 23 | | 92 |
| TOTAL CURRENT LIABILITIES | | 4,395 | | 5,412 |
| Long-term other payables | | 280 | | 47 |
| COMMITMENTS | | | | |
| STOCKHOLDERS EQUITY | | | | |
| Preferred stock - | | | | |
| Authorized, 5,000,000 shares, including 200,000 shares of Series A Junior | | | | |

| | | | | |
|---|---|---|---|---|
| Participating | | | | |
| Issued and outstanding, none | | - | | - |
| Common stock, at stated value - | | | | |
| Authorized, 30,000,000 shares | | | | |
| Issued and outstanding, 9,267,907 | | | | |
| and 9,027,867 shares | | 23,388 | | 22,172 |
| Accumulated earnings | | 1,830 | | 900 |
| Accumulated other comprehensive income | | 1,220 | | 893 |
| TOTAL STOCKHOLDERS EQUITY | | 26,438 | | 23,965 |
| TOTAL LIABILITIES AND STOCKHOLDERS | | | | |
| EQUITY | $ | 31,113 | $ | 29,424 |

*See notes to consolidated financial statements*

**DATA I/O CORPORATION**
**CONSOLIDATED STATEMENTS OF OPERATIONS**
**(in thousands, except per share amounts)**
**UNAUDITED**

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | **2011** | **2010** | **2011** | **2010** |
| Net Sales | $ 6,849 | $ 6,592 | $ 13,892 | $ 12,843 |
| Cost of goods sold | 2,841 | 2,742 | 5,720 | 5,240 |
| Gross margin | 4,008 | 3,850 | 8,172 | 7,603 |
| Operating expenses: | | | | |
| Research and development | 1,276 | 960 | 2,627 | 1,911 |
| Selling, general and administrative | 2,215 | 1,876 | 4,388 | 3,813 |
| Total operating expenses | 3,491 | 2,836 | 7,015 | 5,724 |
| Gain on sale of assets | - | - | - | 3 |
| Operating income | 517 | 1,014 | 1,157 | 1,882 |
| Non-operating income (expense): | | | | |
| Interest income | 19 | 15 | 32 | 17 |
| Interest expense | (1) | (3) | (2) | (6 |
| Foreign currency transaction gain (loss) | (32) | (122) | (66) | (178 |
| Total non-operating income (loss) | (14) | (110) | (36) | (167 |
| Income before income taxes | 503 | 904 | 1,121 | 1,715 |
| Income tax (expense) benefit | (105) | (45) | (191) | (148 |
| Net income | $ 398 | $ 859 | $ 930 | $ 1,567 |
| | | | | |
| Basic earnings per share | $ 0.04 | $ 0.10 | $ 0.10 | $ 0.17 |
| Diluted earnings per share | $ 0.04 | $ 0.09 | $ 0.10 | $ 0.17 |
| Weighted-average basic shares | 9,176 | 8,984 | 9,103 | 8,972 |
| Weighted-average diluted shares | 9,343 | 9,101 | 9,289 | 9,091 |

*See notes to consolidated financial statements*

**DATA I/O CORPORATION**
**CONSOLIDATED STATEMENTS OF CASH FLOWS**
**(in thousands)**
**(UNAUDITED)**

| | Six Months Ended June 30, | |
|---|---|---|
| | **2011** | **2010** |
| **CASH FLOWS FROM OPERATING ACTIVITIES:** | | |
| Net income | $ 930 | $ 1,567 |
| Adjustments to reconcile income to net cash provided by (used in) operating activities: | | |
| Depreciation and amortization | 573 | 562 |
| Gain on sale of assets | - | (3) |
| Equipment transferred to cost of goods sold | 83 | 308 |
| Share-based compensation | 210 | 157 |
| Net change in: | | |
| Trade accounts receivable | (182) | (1,551) |
| Inventories | (313) | 432 |
| Other current assets | 73 | 147 |
| Accrued cost of business restructuring | - | (50) |
| Accounts payable and accrued liabilities | (779) | 429 |
| Deferred revenue | (222) | (17) |
| Other long-term liabilities | 189 | - |
| Deposits and other long-term assets | 59 | (34) |
| Net cash provided by (used in) operating activities | 621 | 1,947 |
| **CASH FLOWS FROM INVESTING ACTIVITIES:** | | |
| Additions to property, plant and equipment | (596) | (580) |
| Net proceeds from sale of assets | - | 3 |
| Purchase of Software Technology | (2,089) | - |
| Cash provided by (used in) investing activities | (2,685) | (577) |
| **CASH FLOWS FROM FINANCING ACTIVITIES:** | | |
| Proceeds from issuance of common stock | 5 | 65 |
| Payment of capital lease obligation | (69) | (63) |
| Cash provided by (used in) financing activities | (64) | 2 |
| Increase (decrease) in cash and cash equivalents | (2,128) | 1,372 |
| Effects of exchange rate changes on cash | 176 | (177) |
| Cash and cash equivalents at beginning of period | 18,942 | 15,642 |
| Cash and cash equivalents at end of period | $ 16,990 | $ 16,837 |
| **Supplemental disclosure of non-cash financing activities:** | | |
| Issuance of common stock for consideration in asset purchase 163,934 shares | $ 1,000 | $ - |

*See notes to consolidated financial statements*

**DATA I/O CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**(UNAUDITED)**

**NOTE 1 - FINANCIAL STATEMENT PREPARATION**

Data I/O prepared the financial statements as of June 30, 2011 and June 30, 2010 according to the rules and regulations of the Securities and Exchange Commission ("SEC"). These statements are unaudited but, in the opinion of management, include all adjustments (consisting of normal recurring adjustments and accruals) necessary to present fairly the results for the periods presented. The balance sheet at December 31, 2010 has been derived from the audited financial statements at that date. We have condensed or omitted certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America according to such SEC rules and regulations. Operating results for the three and six months ended June 30, 2011 are not necessarily indicative of the results that may be expected for the year ending December 31, 2011. These financial statements should be read in conjunction with the annual audited financial statements and the accompanying notes included in the Company's Form 10-K for the year ended December 31, 2010.

Revenue Recognition

Data I/O recognizes revenue at the time of shipment. When arrangements include multiple elements, we use objective evidence of selling price to allocate revenue to the elements and recognize revenue when the criteria for revenue recognition have been met for each element. The amount of revenue recognized is affected by our judgments as to the collectability of the transaction or whether an arrangement includes multiple elements and if so, whether specific objective evidence of selling price exists for those elements.

The revenue related to products requiring installation that is perfunctory is recognized at the time of shipment provided that persuasive evidence of an arrangement exists, shipment has occurred, the price is fixed or determinable, and collectability is reasonably assured. Installation that is considered perfunctory includes any installation that can be performed by other parties, such as distributors, other vendors, or in most cases the customers themselves. This

takes into account the complexity, skill, and training needed as well as customer expectations regarding installation. We measure the standalone selling price of the product versus the service installation value component by the amount paid to independent representative service groups or the amount of additional discount given to independent distributors to provide the service installation.

We record revenue from the sale of service and update contracts as deferred revenue and we recognize it on a straight-line basis over the contractual period, which is typically one year. Service revenue from time and materials contracts and training services are recognized as services are performed. We establish a reserve for sales returns based on historical trends in product returns and estimates for new items. We have a stated return policy that customers can return standard products for any reason within 30 days after delivery, provided that the returned product is received in its original condition, including all packaging materials, for a refund of the price paid less a restocking charge of 30% of the total amount invoiced for the product returned, unless such restocking charge is waived by Data I/O.

On those occasions when we sell software separately, we recognize software revenue upon shipment provided that no significant obligations remain on our part, substantive acceptance conditions, if any, have been met and when the fee is fixed and determinable and when collection is deemed probable.

Certain fixed-price engineering services contracts that require significant production, modification, or customization of software, are accounted for using the percentage-of-completion method. We use the percentage-of-completion method of accounting because it is the most accurate method to recognize revenue based on the nature and scope of certain of our fixed-price engineering services contracts; it is a better measure of periodic income results than other methods and it better matches revenue recognized with the cost incurred. Percentage-of-completion is measured based primarily on input measures such as hours incurred to date compared to total estimated hours at completion, with consideration given to output measures, such as contract milestones, when applicable. Significant judgment is required when estimating total hours and progress to completion on these arrangements, which determines the amount of revenue we recognize as well as whether a loss is recognized, if expected to be incurred upon project completion. Revisions to hour and cost estimates are incorporated in the period in which the facts that give rise to the revision become known.

Stock-Based Compensation Expense

Data I/O measures and recognizes compensation expense as required for all share-based payment awards, including employee stock options and restricted stock awards, based on estimated fair values on the grant dates. Total share-based compensation for the three and six months ended June 30, 2011 was $122,788 and $209,900, respectively. Total share-based compensation for the three and six months ended June 30, 2010 was $82,000 and $157,000, respectively.

Income Tax

Historically when accounting for uncertainty in income taxes, Data I/O has not incurred any interest or penalties associated with tax matters and no interest or penalties were recognized during the three and six months ended June 30, 2011. However, the Company has adopted a policy whereby amounts related to interest and penalties associated with tax matters are classified as general and administrative expense when incurred.

Data I/O has incurred net operating losses in certain past years. We continue to maintain a valuation allowance for the full amount of the net deferred tax asset balance associated with our net operating losses, as sufficient uncertainty exists regarding our ability to realize such tax assets in the future. There was $102,000 of unrecognized tax benefits related to uncertain tax positions and related valuation allowance as of June 30, 2011.

Tax years that remain open for examination include 2007, 2008, 2009 and 2010 in the United States of America. In addition, tax years from 1999 to 2006 may be subject to examination in the event that the Company utilizes the NOL s or other carry forwards from those years in its current or future year tax return.

Recent Accounting Pronouncements

In June 2011, the FASB issued ASU No. 2011-05, *Comprehensive Income (Topic 220): Presentation of Comprehensive Income* ( ASU 2011-05 ). This ASU amends requirements for the presentation of other comprehensive income (OCI), requiring presentation of comprehensive income in either a single, continuous statement of comprehensive income or on separate but consecutive statements, the statement of operations and the statement of OCI. The amendment is effective for the Company at the beginning of fiscal year 2013 with early adoption permitted. The adoption of this guidance will not impact the Company's financial position, results of operations or cash flows and will only impact the presentation of OCI on the financial statements.

In May 2011, the FASB issued ASU No. 2011-04, *Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in US GAAP and International Reporting Standards* ( ASU No. 2011-04 ) which amended the guidance regarding fair value measurement and disclosure. The amended guidance clarifies the application of existing fair value measurement and disclosure requirements. The amendment is effective for the Company at the beginning of January 2012, with early adoption prohibited. The adoption of this amendment is not expected to materially affect the Company's financial statements.

In October 2009, the FASB issued ASU No. 2009-13, *Revenue Recognition (Topic 605): Multiple-Deliverable Revenue Arrangements* ( ASU 2009-13 ). It amends the criteria for separating consideration in multiple-deliverable arrangements. This standard establishes a selling price hierarchy for determining the selling price of a deliverable. The selling price used for each deliverable will be based on vendor-specific objective evidence if available, third-party evidence if vendor-specific objective evidence is not available, or estimated selling price if neither vendor-specific objective evidence nor third-party evidence is available. This standard also replaces the term *fair value* in the revenue allocation guidance with *selling price* to clarify that the allocation of revenue is based on entity-specific assumptions rather than assumptions of a market participant. It also eliminates the residual method of allocation and requires that arrangement consideration be allocated at the inception of the arrangements to all deliverables using the relative selling price method. This standard is effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. The impact of adoption of this standard had no material effect on the accompanying condensed consolidated financial statements.

In October 2009, the FASB issued ASU No. 2009-14, *Software (Topic 985): Certain Revenue Arrangements That Include Software Elements* ( ASU 2009-14 ). According to this update, tangible products containing software components and non-software components that function together to deliver the tangible product s essential functionality are no longer within the scope of the software revenue guidance. It provides additional guidance on how to determine which software, if any, relating to the tangible product also would be excluded from the scope of the software revenue guidance. This standard shall be adopted in the same period using the same transition method as indicated in the update to revenue arrangements with multiple deliverables. The impact of adoption of this standard had no material effect on the accompanying condensed consolidated financial statements.

**NOTE 2 - INVENTORIES**

Inventories consisted of the following components:

| | June 30, 2011 | December 31, 2010 |
|---|---|---|
| (in thousands) | | |
| Raw material | $ 2,510 | $ 2,098 |
| Work-in-process | 1,008 | 772 |
| Finished goods | 408 | 700 |
| Inventories | $ 3,926 | $ 3,570 |

**NOTE 3 PROPERTY AND EQUIPMENT, NET**

Property and equipment consisted of the following components:

| | June 30, 2011 | December 31, 2010 |
|---|---|---|
| (in thousands) | | |
| Leasehold improvements | $ 476 | $ 396 |
| Equipment | 8,459 | 8,264 |
| | 8,935 | 8,660 |
| Less accumulated depreciation | $ 7,665 | $ 7,404 |
| Property and equipment - net | $ 1,270 | $ 1,256 |

**NOTE 4 INTANGIBLE SOFTWARE TECHNOLOGY, NET**

On April 29, 2011, Data I/O purchased software technology for $2 million in cash and 163,934 shares of Data I/O common stock, valued at $1 million on the date of purchase. Acquisition costs of $89,000 were capitalized as part of the transaction. The transaction was accounted for as an asset purchase as it was determined the assets acquired did not constitute an operational business.

For a period of five years Data I/O will pay the seller royalties of 4% of directly associated revenues relating to this acquired software technology. The company will expense the royalty payments when they are incurred as the Company cannot reasonably estimate the future royalty payment amount at the time of the acquisition.

The following is a summary of the company's intangible assets:

| | June 30, 2011 | December 31, 2010 |
|---|---|---|
| (in thousands) | | |
| Intangible software technology | $ 3,089 | $ - |
| Less accumulated amortization | $ 75 | $ - |
| Intangible software technology - net | $ 3,014 | $ - |

**NOTE 5 BUSINESS RESTRUCTURING**

We took restructuring actions in 2008 totaling $542,000, primarily severance-related, and additional actions in 2009 totaling $203,000 to flatten and streamline the organization, as well as reducing cost, by decreasing the size of our Board and abandoning a portion of our building space. At June 30, 2011, all previous accrued restructure costs have been paid or eliminated as a result of our lease amendment in February 2011.

An analysis of the restructuring is as follows (in thousands):

| Restructuring (in thousands) | Reserve Balance 12/31/2009 | 2010 Expense | 2010 Payments/ Write-Offs | Reserve Balance 12/31/2010 | 2011 Expense | 2011 Payments/ Write-Offs | Reserve Balance 6/30/2011 |
|---|---|---|---|---|---|---|---|
| Downsizing US operations: | | | | | | | |
| Facility & other costs | $ 158 | $ - | $ 100 | $ 58 | $ - | $ 58 | $ - |
| Total | $ 158 | $ - | $ 100 | $ 58 | $ - | $ 58 | $ - |

**NOTE 6 OTHER ACCRUED LIABILITIES**

Other accrued liabilities consisted of the following:

| | June 30, 2011 | December 31, 2010 |
|---|---|---|
| (in thousands) | | |
| Product warranty | $ 398 | $ 376 |
| Sales return reserve | 89 | 66 |
| Other taxes | 109 | 109 |
| Other | 204 | 219 |
| Other accrued liabilities | $ 800 | $ 770 |

The changes in Data I/O s product warranty liability for the six months ending June 30, 2011 are as follows:

| | June 30, 2011 |
|---|---|
| (in thousands) | |
| Liability, beginning balance | $ 376 |
| Net expenses | 388 |
| Warranty claims | (388) |
| Accrual revisions | 22 |
| Liability, ending balance | $ 398 |

**NOTE 7 OPERATING LEASE AND OTHER COMMITMENTS**

Data I/O has purchase obligations for inventory and production costs as well as other obligations such as capital expenditures, service contracts, marketing, and development agreements. Arrangements are considered purchase obligations if a contract specifies all significant terms, including fixed or minimum quantities to be purchased, a pricing structure and approximate timing of the transaction. Most arrangements are cancelable without a significant penalty, and with short notice, typically less than 90 days. At June 30, 2011, the purchase and other obligations totaled $1,379,000.

Data I/O also has commitments under non-cancelable operating leases. In February 2011, we entered into an amended lease arrangement that reduced the amount of space leased in Redmond and extended the lease term through June 20, 2016. In June 2011, we entered into a new two-year lease for our Shanghai office. These amended terms are included in the operating lease table below.

Future annual lease payments at June 30, 2011:

| (in thousands) | Operating Leases |
|---|---|
| 2011 | $ 576 |
| 2012 | 1,158 |
| 2013 | 987 |
| 2014 | 862 |
| 2015 | 805 |
| Thereafter | 394 |
| Total | $ 4,782 |

**NOTE 8 CONTINGENCIES**

As of June 30, 2011, Data I/O was not a party to any material pending legal proceedings, other than ordinary routine litigation incidental to the business.

**NOTE 9 LONG-TERM DEBT**

On September 27, 2006, the Company entered into a five year capital lease agreement in the amount of $591,145. The imputed interest rate is 7.69%. At June 30, 2011, scheduled maturities of the capital lease obligation for the years ending December 31 are as follows:

| | Long-Term Debt |
|---|---|
| (in thousands) | |
| 2011 | $24 |
| 2012 | - |
| Total minimum lease payments | $24 |
| Less: Amount representing interest | (1) |
| Present value of capital lease obligation | $23 |
| Current portion of long-term debt | (23) |
| Non-current portion of long-term debt | $ - |

**NOTE 10 EARNINGS PER SHARE**

Basic earnings (loss) per share is calculated based on the weighted average number of common shares outstanding during each period. Diluted earnings per share is calculated based on these same weighted average shares outstanding plus the effect of potential shares issuable upon assumed exercise of stock options based on the treasury stock method. Potential shares issuable upon the exercise of stock options are excluded from the calculation of diluted earnings per share to the extent their effect would be anti-dilutive.

The following table sets forth the computation of basic and diluted earnings per share:

| | Three Months Ended | Six Months Ended |
|---|---|---|

| (in thousands except per share data) | June 30, 2011 | June 30, 2010 | June 30, 2011 | June 30, 2010 |
|---|---|---|---|---|
| Numerator for basic and diluted earnings per share: | | | | |
| Net income | $ 398 | $ 859 | $ 930 | $ 1,567 |
| Denominator for basic earnings per share - weighted-average shares | 9,176 | 8,984 | 9,103 | 8,972 |
| Employee stock options and awards | 167 | 117 | 186 | 119 |
| Denominator for diluted earnings per share - adjusted weighted-average shares and assumed conversions of stock options | 9,343 | 9,101 | 9,289 | 9,091 |
| Basic and diluted earnings per share: | | | | |
| Total basic earnings per share | $ 0.04 | $ 0.10 | $ 0.10 | $ 0.17 |
| Total diluted earnings per share | $ 0.04 | $ 0.09 | $ 0.10 | $ 0.17 |

The computation for the three and six months ended June 30, 2011 excludes 310,209 and 223,362 options, respectively, to purchase common stock as their effect is anti-dilutive. The computation for the three and six months ended June 30, 2010 excludes 257,401 and 199,273 options, respectively, to purchase common stock as their effect is anti-dilutive.

**NOTE 11 SHARE-BASED COMPENSATION**

The impact on our results of operations of recording share-based compensation for the three and six months ended June 30, 2011 and

June 30, 2010, respectively, are as follows:

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | June 30, 2011 | June 30, 2010 | June 30, 2011 | June 30, 2010 |
| (in thousands) | | | | |
| Cost of goods sold | $ 12 | $ 6 | $ 21 | $ 13 |
| Research and development | 23 | 11 | 32 | 18 |
| Selling, general and administrative | 88 | 65 | 157 | 126 |
| Total share-based compensation | $ 123 | $ 82 | $ 210 | $ 157 |
| | | | | |
| Impact on net income (loss) per share: | | | | |
| Basic and diluted | $ (0.01) | $ (0.01) | $ (0.02) | $ (0.02) |

The fair value of share-based awards for employee stock options was estimated using the Black-Scholes valuation model. The following weighted average assumptions were used to calculate the fair value of stock options granted during the three months and six months ended June 30, 2011 and 2010:

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | June 30, 2011 | June 30, 2010 | June 30, 2011 | June 30, 2010 |
| Risk-free interest rates | 1.41% | 1.80% | 1.40% | 1.80% |
| Volatility factors | 0.55 | 0.56 | 0.55 | 0.56 |
| Expected life of the option in years | 4.00 | 4.00 | 4.00 | 4.00 |
| Expected dividend yield | None | None | None | None |

Option grants during the six months ended June 30, 2011 were 322,000.

At June 30, 2011, there remained approximately $1,454,699 of unamortized expected future compensation expense associated with unvested option grants and restricted stock awards, with a remaining weighted average amortization

period of 3.04 years.

**NOTE 12 COMPREHENSIVE INCOME (LOSS)**

For the three and six months ended June 30, 2011 and June 30, 2010, total comprehensive income (loss) was comprised of the following:

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | June 30, 2011 | June 30, 2010 | June 30, 2011 | June 30, 2010 |
| (in thousands) | | | | |
| Net income | $ 398 | $ 859 | $ 930 | $ 1,567 |
| Foreign currency translation gain (loss) | 128 | (228) | 327 | (325) |
| Total comprehensive income (loss) | $ 526 | $ 631 | $ 1,257 | $ 1,242 |

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

General

**Forward-Looking Statements**

This Quarterly Report on Form 10-Q includes forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. This Act provides a safe harbor for forward-looking statements to encourage companies to provide prospective information about themselves as long as they identify these statements as forward-looking and provide meaningful cautionary statements identifying important factors that could cause actual results to differ from the projected results. All statements other than statements of historical fact made in this Quarterly Report on Form 10-Q are forward-looking. In particular, statements herein regarding industry prospects or trends; expected revenues; expected level of expense; future results of operations, restructuring implications; breakeven point, or financial position; changes in gross margin; economic conditions and capital spending outlook; market acceptance of our newly introduced or upgraded products; development, introduction and shipment of new products; and any other guidance on future periods are forward-looking statements. Forward-looking statements reflect management s current expectations and are inherently uncertain. Although Data I/O believes that the expectations reflected in these forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance, achievements, or other future events. Moreover, neither Data I/O nor anyone else assumes responsibility for the accuracy and completeness of these forward-looking statements. Data I/O is under no duty to update any of these forward-looking statements after the date of this report. The reader should not place undue reliance on these forward-looking statements. The discussions above and in the section in Item 1A., Risk Factors in the Quarterly report on Form 10-Q and in Item 1A., Risk Factors Cautionary Factors That May Affect Future Results in the Company s Annual report on Form 10-K for the year ended December 31, 2010 describe some, but not all, of the factors that could cause these differences.

**OVERVIEW**

We continued to focus on our primary goal of managing the business to grow profits, while developing, launching and enhancing products to drive revenue and earnings growth. Our challenge continues to be operating in a cyclical and rapidly evolving industry environment. We are continuing our efforts to balance business geography shifts, increasing costs and strategic investments in our business with the level of demand and mix of business we expect.

Data I/O purchased software technology for $2 million in cash and 163,934 shares (approximately $1 million) of company common stock on April 29, 2011 and capitalized $89,000 of acquisition costs. Also, we will pay the seller

royalties of 4% of directly associated revenues for a period of 5 years. This software technology will be used in our internal product development, incorporated into new products currently in development, and will be the basis for new software offerings in adjacent market spaces.

We are focusing our research and development efforts in our strategic growth markets, namely new programming technology, software, and automated programming systems for the manufacturing environment, as well as reconnecting with our traditional market, the design engineer with design tools. We continue to focus on extending the capabilities and support for our FlashCORE architecture, and the ProLINE-RoadRunner, FLX, PS, and FlashPAK product lines, as well as new product initiatives. Our applications innovation strategy provides complete solutions to target customer s business problems. These solutions generally have a larger software element, may involve third-party components, and in many cases, will be developed or customized to address the specific requirements of individual customers. We believe by adding these features and applications to our strategic product platforms, we will be able to set ourselves apart from other product suppliers and elevate our relationships with our customers.

Our customer focus has been on strategic high volume manufacturers in key market segments like wireless, automotive, industrial controls and programming centers and supporting NAND Flash and microcontrollers on our newer products to gain new accounts. We also provide product solutions used by electronics design engineers. We continued to expand our China operations to take advantage of the growth of manufacturing in China and to operate close to our customers. We continued to address the effectiveness of our sales and marketing organization and sales channels by adding and changing channels and providing our channel partners with extensive product, sales and service training. We recognized the need to diversify our customer base and are continuing to take steps to broaden our channels of distribution and representation to reach a greater number of customers. We believe these channel actions help us grow our business more rapidly, both by adding new customers and by increasing penetration of existing accounts.

**cRITICAL aCCOUNTING pOLICY jUDGMENTS AND eSTIMATES**

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires that we make estimates and judgments, which affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities. On an on-going basis, Data I/O evaluates our estimates, including those related to revenue recognition, estimating the percentage-of-completion on fixed-price professional engineering service contracts, sales returns, bad debts, inventories, intangible assets, income taxes, warranty obligations, contingencies such as litigation, and contract terms that have multiple elements and other complexities typical in the capital equipment industry. We base our estimates on historical experience and other assumptions that we believe are reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions.

Data I/O believes the following critical accounting policies affect the more significant judgments and estimates used in the preparation of our financial statements:

Revenue Recognition: Sales of Data I/O s semiconductor programming equipment are recognized at the time of shipment. We have determined that our automated products have reached a point of maturity and stability such that product acceptance can be assured by testing at the factory prior to shipment and that the installation meets the criteria to be considered a separate element. These systems are standard products with published product specifications and are configurable with standard options. The evidence that these systems could be accepted was based upon having standardized factory production of the units, results from batteries of tests of product performance to our published specifications, quality inspections and installation standardization, as well as past product operation validation with customers and the history provided by our installed base of products upon which the current versions were based. When arrangements include multiple elements, we use objective evidence of selling price to allocate revenue to the various elements and recognize revenue when the criteria for revenue recognition have been met for each element. Effective January 1, 2011, under the provision of ASU 2009-13 Revenue Recognition (Topic 605), the allocation of revenue is done on a pro-rata versus residual basis for the recognized revenue. The amount of revenue recognized is affected by our judgments as to the collectability of the transaction or whether an arrangement includes multiple elements and if so, whether specific objective evidence of selling price exists for those elements. The measure of standalone selling price of the product versus the service installation value component is determined by the amount Data I/O pays to independent representative service groups or the amount of additional discount given to independent distributors, to provide the service installation. Changes to the elements in an arrangement and the ability to establish specific objective evidence for those elements could affect the timing of the revenue recognition. These conditions could be subjective and actual results could vary from the estimated outcome.

Installation that is considered perfunctory includes any installation that can be performed by other parties, such as distributors, other vendors, or in most cases the customer themselves. This takes into account the complexity, skill, and training needed as well as customer expectations regarding installation. The revenue related to products requiring installation that is perfunctory is recognized at the time of shipment provided that persuasive evidence of an arrangement exists, shipment has occurred, the price is fixed or determinable, and collectability is reasonably assured.

We record revenue from the sale of service and update contracts as deferred revenue and we recognize it on a straight-line basis over the contractual period, which is typically one year. Service revenue from time and materials contracts and training services is recognized as services are performed. We recognize software revenue upon shipment provided that no significant obligations remain on our part, substantive acceptance conditions, if any, have been met and when the fee is fixed and determinable and when collection is deemed probable.

Certain fixed-price engineering service contracts that require significant production, modification, or customization of software, are accounted for using the percentage-of-completion method. We use the percentage-of-completion method of accounting because it is the most accurate method to recognize revenue based on the nature and scope of our fixed-price professional engineering service contracts; it is a better measure of periodic income results than other methods and it better matches revenue recognized with the costs incurred. Percentage-of-completion is measured based primarily on input measures such as hours incurred to date compared to total estimated hours to complete, with consideration given to output measures, such as contract milestones, when applicable. Significant judgment is required when estimating total hours and progress to completion on these arrangements, which determines the amount of revenue we recognize as well as whether a loss is recognized if one is expected to be incurred upon project completion. Revisions to hour and cost estimates are incorporated in the period the amounts are recognized if the results of the period have not been reported; otherwise, the revision of estimates are recognized in the period in which the facts that give rise to the revision become known.

We establish a reserve for sales returns based on historical trends in product returns and estimates for new items. Data I/O has a stated return policy that customers can return standard products for any reason within 30 days after delivery provided that the returned product is received in its original condition, including all packaging materials, for a refund of the price paid less a restocking charge of 30% of the total amount invoiced for the product returned, unless such restocking charge is waived in writing by Data I/O. For us to recognize revenue, the price is fixed or determinable at the date of the sale, the buyer has paid or is obligated to pay and the obligation is not contingent on resale of the product, the buyer s obligation would not be changed in the event of theft, physical destruction or damage to the product, the buyer acquiring the product for resale has economic substance apart from Data I/O and we have no contractual obligations for future performance to directly bring about the resale of the product by the buyer.

Allowance for Doubtful Accounts: We base the allowance for doubtful accounts receivable on our assessment of the collectability of specific customer accounts and the aging of accounts receivable. If there is deterioration of a major customer s credit worthiness or actual defaults are higher than historical experience, our estimates of the recoverability of amounts due to us could be adversely affected.

Inventory: Inventories are stated at the lower of cost or market. Adjustments are made to standard cost, which approximates actual cost on a first-in, first-out basis. We estimate reductions to inventory for obsolete, slow-moving, excess and non-salable inventory by reviewing current transactions and forecasted product demand. We evaluate our inventories on an item by item basis and record inventory adjustments accordingly. If there is a significant decrease in demand for our products or there is a higher risk of inventory obsolescence because of rapidly changing technology and customer requirements, Data I/O may be required to increase our inventory adjustments and our gross margin could be adversely affected.

Warranty Accruals: Data I/O accrues for warranty costs based on the expected material and labor costs to fulfill our warranty obligations. If we experience an increase in warranty claims, which are higher than our historical experience, our gross margin could be adversely affected.

Tax Valuation Allowances: Given the uncertainty created by our loss history, as well as the current uncertain economic outlook for our industry and capital spending, Data I/O expects to continue to limit the recognition of net deferred tax assets and accounting for uncertain tax positions and maintain the tax valuation allowances. We expect, therefore, that reversals of the tax valuation allowance will take place only as we are able to take advantage of the underlying tax loss or other attributes in carry forward. The transfer pricing and expense or cost sharing arrangements are complex areas where judgments, such as the determination of arms-length arrangements, can be subject to challenges by different tax jurisdictions.

Share-based Compensation: We account for share-based awards made to our employees and directors, including employee stock option awards and restricted and performance share awards, using the estimated grant date fair value method of accounting. We estimate the fair value using the Black-Scholes valuation model, which requires the input of highly subjective assumptions, including the option s expected life, forfeiture rate, and the price volatility of the underlying stock. The expected stock price volatility assumption was determined using the historical volatility of the Company s common stock. Changes in the subjective assumptions required in the valuation model may significantly affect the estimated value of the awards, the related stock-based compensation expense and, consequently, our results of operations. Beginning in the second quarter of 2006, restricted stock awards were granted. Employee Stock Purchase Plan ( ESPP) shares were issued under provisions that do not require us to record any equity compensation expense.

Results of Operations

**Net Sales**

| Net sales by product line (in thousands) | Three Months Ended June 30, 2011 | Change | June 30, 2010 | Six Months Ended June 30, 2011 | Change | June 30, 2010 |
|---|---|---|---|---|---|---|
| Automated programming systems | $ 4,050 | (3.8%) | $ 4,209 | $ 8,832 | 5.5% | $ 8,375 |
| Non-automated programming systems | 2,799 | 17.5% | 2,383 | 5,060 | 13.2% | 4,468 |
| Total programming systems | $ 6,849 | 3.9% | $ 6,592 | $ 13,892 | 8.2% | $ 12,843 |

| Net sales by location (in thousands) | June 30, 2011 | Change | June 30, 2010 | June 30, 2011 | Change | June 30, 2010 |
|---|---|---|---|---|---|---|
| United States | $ 584 | (28.7%) | $ 819 | $ 1,114 | (25.0%) | $ 1,485 |
| % of total | 8.5% | | 12.4% | 8.0% | | 11.6% |
| International | $ 6,265 | 8.5% | $ 5,773 | $ 12,778 | 12.5% | $ 11,358 |
| % of total | 91.5% | | 87.6% | 92.0% | | 88.4% |

Revenues for the second quarter of 2011 were $6.8 million, up 4% compared with $6.6 million in the second quarter of 2010, but down sequentially from $7 million in the first quarter of 2011. On a regional basis, Asia had strong growth in the second quarter of 2011, with revenue growth of 48%, while revenue from Europe declined 3%, and the revenue from the Americas declined 26%, compared to the second quarter of 2010. The Americas revenue was impacted by a continued decline in sales in Mexico and lower custom software sales, but on a sequential basis, revenue from the Americas increased 24% over the first quarter of 2011.

For the first six months of 2011 compared to 2010, the increase in sales reflected the same factors as the second quarter, namely strong Asia sales which drove non-automated sales of FlaskPaks, and declining Americas sales due to lower custom software sales and lower sales in Mexico.

Second quarter 2011 order bookings increased 11% to $7.3 million from $6.5 million in the same period last year and increased 19% sequentially from $6.1 million in the first quarter of 2011. Data I/O ended the quarter with a backlog of $1.4 million at the end of the second quarter of 2010 compared to $0.9 million at March 31, 2011 and $1.4 million at June 30, 2010.

**Gross Margin**

| | Three Months Ended | | | Six Months Ended | | |
|---|---|---|---|---|---|---|
| Net sales by product line (in thousands) | June 30, 2011 | Change | June 30, 2010 | June 30, 2011 | Change | June 30, 2010 |
| Gross margin | $ 4,008 | 4.1% | $ 3,850 | $ 8,172 | 7.5% | $ 7,603 |
| Percentage of net sales | 58.5% | | 58.4% | 58.8% | | 59.2% |

Gross margin as a percentage of sales in the second quarter of 2011 was 58.5 %, compared with 58.4% in the second quarter of 2010 and 59.1 % in the first quarter of 2011. The decrease compared to the first quarter of 2011 was primarily due to the product mix, increased service labor costs and engineering contract software costs, offset in part by less unfavorable factory variances.

Gross margin as a percentage of net sales for the first six months of 2011 was 58.8 %, compared with 59.2% for the first six months of 2010. The decrease was primarily due to the product mix, increased service labor costs and engineering contract software costs, offset in part by less unfavorable factory variances.

**Research and Development**

| | Three Months Ended | | | Six Months Ended | | |
|---|---|---|---|---|---|---|
| | June 30, 2011 | Change | June 30, 2010 | June 30, 2011 | Change | June 30, 2010 |
| (in thousands) | | | | | | |
| Research and development | $ 1,276 | 32.9% | $ 960 | $ 2,627 | 37.5% | $ 1,911 |
| Percentage of net sales | 18.6% | | 14.6% | 18.9% | | 14.9% |

Research and development ( R&D ) spending for the second quarter of 2011 increased by $316,000 compared to the second quarter of 2010 due primarily to the use of outside resources to accelerate our growth initiatives and due to $94,000 less engineering costs absorbed by operations on custom software development contracts. Also included in second quarter 2011 R&D expense was two months amortization expense of $73,000 associated with the software technology acquisition. Next quarter will include 3 months of amortization. However, overall R&D expense in the second quarter was actually down $77,000 sequentially from the first quarter of 2011 primarily due to fewer materials used.

R&D expenses increased $716,000 for the first six months of 2011 compared to the same period in 2010, primarily due to the use of outside resources to accelerate our growth initiatives, as well as higher personnel costs and $104,000 less engineering costs absorbed by operations on custom software development contracts.

**Selling, General and Administrative**

| | Three Months Ended | | | Six Months Ended | | |
|---|---|---|---|---|---|---|
| | June 30, 2011 | Change | June 30, 2010 | June 30, 2011 | Change | June 30, 2010 |
| (in thousands) | | | | | | |
| Selling, general & administrative | $ 2,215 | 18.1% | $ 1,876 | $ 4,388 | 15.1% | $ 3,813 |
| Percentage of net sales | 32.3% | | 28.5% | 31.6% | | 29.7% |

Selling, general and administrative ( SG&A ) expenses increased $339,000 in the second quarter of 2011compared to the same period in 2010, due to increased use of outside professional consultants, higher compensation and travel costs, offset by $169,000 of lower incentive compensation. SG&A was sequentially flat compared to the first quarter of 2011, but we had higher marketing costs due to software technology related personnel additions; higher sales travel and retirement transition compensation; and higher consulting fees, which were offset by lower audit fees and public company costs. Two consulting projects that had approximately $90,000 of expense in the second quarter (including the TM Capital Engagement) were completed in July and will result in lower costs going forward.

SG&A expenses increased $575,000 for the first six months of 2011 compared to the same period in 2010, again due to increased use of outside professional consultants, higher compensation and travel costs, offset by $203,000 of lower incentive compensation.

**Interest**

| | Three Months Ended | | | Six Months Ended | | |
|---|---|---|---|---|---|---|
| | June 30, 2011 | Change | June 30, 2010 | June 30, 2011 | Change | June 30, 2010 |
| (in thousands) | | | | | | |
| Interest Income | $ 19 | 26.7% | $ 15 | $ 32 | 88.2% | $ 17 |
| Interest expense | $ (1) | (66.7%) | $ (3) | $ (2) | (66.7%) | $ (6) |

Interest income for the three and six months ended June 30, 2011 increased compared to the same period in 2010 due to higher cash balances. Interest expense decreased for the three and six months ended June 30, 2011 compared to the same period in 2010 as a result of the lower balance on the equipment capital lease.

**Income Taxes**

| | Three Months Ended | | | Six Months Ended | | |
|---|---|---|---|---|---|---|
| | June 30, 2011 | Change | June 30, 2010 | June 30, 2011 | Change | June 30, 2010 |
| (in thousands) | | | | | | |
| Income tax (expense) benefit | $ (105) | 133.3% | $ (45) | $ (191) | 29.1% | $ (148) |

Income tax expense recorded for the second quarter and first six months of 2011 and 2010 resulted from foreign and state taxes. The effective tax rate differed from the statutory tax rate primarily due to the effect of valuation allowances and state taxes. Data I/O has a valuation allowance of $9,093,000 as of June 30, 2011. Our deferred tax assets and valuation allowance are reduced by approximately $102,000 associated with the requirements of accounting for uncertain tax positions as of June 30, 2011.

Financial Condition

**Liquidity and Capital Resources**

| | June 30, 2011 | Change | December 31, 2010 |
|---|---|---|---|
| (in thousands) | | | |
| Working capital | $ 22,332 | $ (271) | $ 22,603 |

Our cash and cash equivalents at June 30, 2011 was $17.0 million, which decreased by approximately $2.0 million due to cash used in the software technology acquisition on April 29, 2011. Accounts receivable decreased to $5.3 million at June 30, 2011 compared to $5.5 million at March 31, 2011. Inventories increased to $3.9 million at June 30, 2011, from $3.5 million at March 31, 2011 due to materials for new product initiatives and in response to certain suppliers longer lead times. Deferred revenue was $1.4 million at June 30, 2011 compared to $1.6 million at March 31, 2011.

We expect that we will continue to make capital expenditures to support our business. Capital expenditures are expected to be funded by existing and internally generated funds or lease financing.

As a result of our significant product development, customer support, international expansion and selling and marketing efforts, we have required substantial working capital to fund our operations. Over the last few years, we restructured our operations to lower our costs and operating expenditures in some geographic regions, while investing in other regions, and to lower the level of revenue required for our net income breakeven point, to preserve our cash position and to focus on profitable operations. We believe that we have sufficient working capital available under our operating plan to fund our operations and capital requirements through at least the next one-year period. Our working capital may be used to fund growth initiatives, including acquisitions, which could reduce our liquidity. Any substantial inability to achieve our current business plan could have a material adverse impact on our financial position, liquidity, or results of operations and may require us to reduce expenditures and/or seek additional financing.

**Long-Term Debt**

During the third quarter of 2006, the Company entered into a five-year capital lease agreement in the amount of $591,145. The lease was used to fund new equipment and installation associated with our move to the new facility in July of 2006. As of June 30, 2011 and December 31, 2010, there is no amount remaining classified as long term debt, and the current portion of long-term debt is $23,000 and $92,000, respectively. See Note 9, Long-Term Debt.

**OFF-Balance sheet arrangements**

Except as noted above in Note 7, Operating Lease and Other Commitments, Data I/O had no off-balance sheet arrangements.

**RECENT ACCOUNTING PRONOUNCEMENTS**

In June 2011, the FASB issued ASU No. 2011-05, *Comprehensive Income (Topic 220): Presentation of Comprehensive Income* ( ASU 2011-05 ). This ASU amends requirements for the presentation of other comprehensive income (OCI), requiring presentation of comprehensive income in either a single, continuous statement of comprehensive income or on separate but consecutive statements, the statement of operations and the statement of OCI. The amendment is effective for the Company at the beginning of fiscal year 2013 with early adoption permitted. The adoption of this guidance will not impact the Company's financial position, results of operations or cash flows and will only impact the presentation of OCI on the financial statements.

In May 2011, the FASB issued ASU No. 2011-04, *Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in US GAAP and International Reporting Standards* ( ASU No. 2011-04 ) which amended the guidance regarding fair value measurement and disclosure. The amended guidance clarifies the application of existing fair value measurement and disclosure requirements. The amendment is effective for the Company at the beginning of January 2012, with early adoption prohibited. The adoption of this amendment is not expected to materially affect the Company's financial statements.

In October 2009, the FASB issued ASU No. 2009-13, *Revenue Recognition (Topic 605): Multiple-Deliverable Revenue Arrangements* ( ASU 2009-13 ). It amends the criteria for separating consideration in multiple-deliverable arrangements. This standard establishes a selling price hierarchy for determining the selling price of a deliverable. The selling price used for each deliverable will be based on vendor-specific objective evidence if available, third-party evidence if vendor-specific objective evidence is not available, or estimated selling price if neither vendor-specific objective evidence nor third-party evidence is available. This standard also replaces the term *fair value* in the revenue allocation guidance with *selling price* to clarify that the allocation of revenue is based on entity-specific assumptions rather than assumptions of a market participant. It also eliminates the residual method of allocation and requires that arrangement consideration be allocated at the inception of the arrangements to all deliverables using the relative selling price method. This standard is effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. The impact of adoption of this standard had no material effect on the accompanying condensed consolidated financial statements.

In October 2009, the FASB issued ASU No. 2009-14, *Software (Topic 985): Certain Revenue Arrangements That Include Software Elements* ( ASU 2009-14 ). According to this update, tangible products containing software components and non-software components that function together to deliver the tangible product s essential functionality are no longer within the scope of the software revenue guidance. It provides additional guidance on how to determine which software, if any, relating to the tangible product also would be excluded from the scope of the software revenue guidance. This standard shall be adopted in the same period using the same transition method as indicated in the update to revenue arrangements with multiple deliverables. The impact of adoption of this standard had no material effect on the accompanying condensed consolidated financial statements.

**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

Not applicable.

## Item 4. Controls and Procedures

**Evaluation of disclosure controls and procedures**

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, Data I/O evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) and Rule 15d-15(e) under the Exchange Act) as of the end of the period covered by this report (the Evaluation Date ). Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that, as of the Evaluation Date, our disclosure controls and procedures were effective at the reasonable level of assurance. Disclosure Controls are controls and procedures designed to reasonably assure that information required to be disclosed in our reports filed under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the SEC s rules and forms. Disclosure Controls are also designed to reasonably assure that such information is accumulated and communicated to our management, including the CEO and CFO, as appropriate to allow timely decisions regarding required disclosure.

**Changes in internal controls**

There were no changes made in our internal controls during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**PART II - OTHER INFORMATION**

**Item 1. Legal Proceedings**

From time to time, we may be involved in litigation relating to claims arising out of our operations in the normal course of business.

As of June 30, 2011, Data I/O was not a party to any material pending legal proceedings, other than ordinary routine litigation incidental to the business.

**Item 1A. Risk Factors**

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2010, which could materially affect our business, financial condition or future results. The risks described in our Annual Report on Form 10-K are not the only risks facing our Company. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results. Other than the following item, there are no material changes to the Risk Factors described in our Annual Report:

Our recent acquisition of assets may have an adverse effect on our business if we cannot develop products on a timely basis or advance our business strategy.

We recently completed an acquisition of software technology assets and expect to invest resources to develop those assets. Development of this software technology investment involves significant challenges and risks including that the transaction does not advance our business strategy; that we do not realize a satisfactory return on our investment; or that we experience difficulty in the integration of new employees, development of the software and technology, or diversion of management s attention from our other business. These events could harm our operating results or financial condition.

**Item 2. Unregistered Sales of Equity Securities, Use of Proceeds**

None

**Item 3. Defaults Upon Senior Securities**

None

**Item 4. [Removed and Reserved]**

**Item 5. Other Information**

None

**Item 6. Exhibits**

(a) **Exhibits**

3 **Articles of Incorporation**:

3.2 Data I/O s Amended and Restated Bylaws as of July 20, 2011 (Incorporated by reference to Data I/O s Current Report on Form 8-K filed July 26, 2011).

10 **Material Contracts:**

10.21 Asset Purchase Agreement dated April 29, 2011, with the Miller Trust, for acquisition of Software Technology (Incorporated by reference to Data I/O s Current Report on Form 8-K filed May 3, 2011).*

31 **Certification Section 302:**

31.1 Chief Executive Officer Certification

31.2 Chief Financial Officer Certification

32 **Certification Section 906:**

32.1 Chief Executive Officer Certification

32.2 Chief Financial Officer Certification

*Portions of this exhibit have been omitted based on an application for confidential treatment from the SEC. The omitted portions of these exhibits have been filed separately with the SEC. Schedules to the Asset Purchase Agreement have been omitted pursuant to Item 601(b)(2) of Regulation S-K. The registrant undertakes to furnish on a supplemental basis a copy of any omitted schedules to the Securities and Exchange Commission upon request.

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**DATA I/O CORPORATION**

(REGISTRANT)

DATED: August 5, 2011

By: //S//Joel S. Hatlen
Joel S. Hatlen
Vice President - Finance
Chief Financial Officer
Secretary and Treasurer
(Principal Financial Officer and Duly Authorized Officer)

By: //S//Frederick R. Hume
Frederick R. Hume
President
Chief Executive Officer

(Principal Executive Officer and Duly Authorized Officer)



Item 3. Quantitative and Qualitative Disclosures About Market Risk 40

Exhibit 31.1

Section 302(a) of the Sarbanes-Oxley Act of 2002

I, Frederick R. Hume, certify that:

1) I have reviewed this quarterly report on Form 10-Q of Data I/O Corporation;

2) Based upon my knowledge, this report does not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3) Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4) The registrant s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c) Evaluated the effectiveness of the registrant s disclosure controls and procedures and presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this quarterly report based on such evaluation; and

d) Disclosed in this quarterly report any change in the registrant s internal control over financial reporting that occurred during the registrant s most recent fiscal quarter (the registrant s fourth fiscal quarter in the case of an annual report) that has materially affected or is reasonably likely to materially affect, the registrant s internal control over financial reporting.

5) The registrant s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant s auditors and the audit committee of registrant s board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant s ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant s internal controls over financial reporting.

DATED: August 5, 2011

/s/ Frederick R. Hume
Frederick R. Hume
Chief Executive Officer
(Principal Executive Officer)

Exhibit 31.2

Section 302(a) of the Sarbanes-Oxley Act of 2002

I, Joel S. Hatlen, certify that:

1) I have reviewed this quarterly report on Form 10-Q of Data I/O Corporation;

2) Based upon my knowledge, this report does not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3) Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4) The registrant s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purpose in accordance with generally accepted accounting principles;

c) Evaluated the effectiveness of the registrant s disclosure controls and procedures and presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this quarterly report based on such evaluation; and

d) Disclosed in this quarterly report any change in the registrant s internal control over financial reporting that occurred during the registrant s most recent fiscal quarter (the registrant s fourth fiscal quarter in the case of an annual report) that has materially affected or is reasonably likely to materially affect, the registrant s internal control over financial reporting.

5) The registrant s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant s auditors and the audit committee of registrant s board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant s ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant s internal controls over financial reporting.

DATED: August 5, 2011

/s/ Joel S. Hatlen
Joel S. Hatlen
Chief Financial Officer
(Principal Financial Officer)

Exhibit 32.1

Certification by Chief Executive Officer

Pursuant to 18 U.S.C. Section 1350

As Adopted Pursuant to

Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the quarterly report of Data I/O Corporation (the Company ) on Form 10-Q for the period ended June 30, 2011 as filed with the Securities and Exchange Commission on the date hereof (the Report ), I, Frederick R. Hume, Chief Executive Officer of the Company, certify, that pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 as amended; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Frederick R. Hume
Frederick R. Hume
Chief Executive Officer
(Principal Executive Officer)
August 5, 2011

Exhibit 32.2

Certification by Chief Financial Officer

Pursuant to 18 U.S.C. Section 1350

As Adopted Pursuant to

Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the quarterly report of Data I/O Corporation (the Company ) on Form 10-Q for the period ended June 30, 2011 as filed with the Securities and Exchange Commission on the date hereof (the Report ), I, Joel S. Hatlen, Chief Financial Officer of the Company, certify, that pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 as amended; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Joel S. Hatlen
Joel S. Hatlen
Chief Financial Officer
(Principal Financial Officer)
August 5, 2011