DATA I/O CORP
Form 10-Q
May 14, 2010

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One) QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES

EXCHANGE ACT OF 1934

(X)
For the quarter ended **March 31, 2010**

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)

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

Title of each class	Name of each exchange on which registered
Common Stock (No Par Value)	Nasdaq Capital Market

Securities registered pursuant to Section 12(g) of the Act
None

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 Website, 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 __ 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 May 12, 2010:

8,979,199

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DATA I/O CORPORATION

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PART I - FINANCIAL INFORMATION

Item 1. **Financial Statements**

DATA I/O CORPORATION
CONSOLIDATED BALANCE SHEETS

	March 31, 2010	December 31, 2009
(in thousands, except share data)		
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 15,684	$ 15,642
Trade accounts receivable, net of allowance for doubtful accounts of $153 and $171	4,727	3,192
Inventories	3,745	3,947
Other current assets	341	434
TOTAL CURRENT ASSETS	24,497	23,215
Property, plant and equipment net	1,741	1,819
Other assets	98	102
TOTAL ASSETS	$ 26,336	$ 25,136
LIABILITIES AND STOCKHOLDERS EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$ 1,242	$ 970
Accrued compensation	880	1,010
Deferred revenue	1,752	1,462
Other accrued liabilities	770	714
Accrued costs of business restructuring	100	100
Income taxes payable	163	91
Current portion long-term debt	134	132
TOTAL CURRENT LIABILITIES	5,041	4,479
Long-term other payables	39	69
Long-term debt	57	90
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, 8,963,106 and 8,955,885 shares		21,848		21,758
Accumulated deficit		(1,403)		(2,112)
Accumulated other comprehensive income		754		852
TOTAL STOCKHOLDERS EQUITY		21,199		20,498
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$	26,336	$	25,136

See notes to consolidated financial statements

DATA I/O CORPORATION

CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

For the three months ended March 31,	2010	2009
(in thousands, except earnings per share data)		
Net Sales	$ 6,252	$ 4,383
Cost of goods sold	2,499	1,940
Gross margin	3,753	2,443
Operating expenses:		
Research and development	950	1,033
Selling, general and administrative	1,938	1,676
Provision for business restructuring	-	22
Total operating expenses	2,888	2,731
Gain on sale of assets	3	1
Operating income (loss)	868	(287)
Non-operating income (expense):		
Interest income	2	4
Interest expense	(3)	(6)
Foreign currency transaction gain (loss)	(56)	(47)
Total non-operating income (loss)	(57)	(49)
Income (loss) before income taxes	811	(336)
Income tax (expense) benefit	(102)	(128)
Net income (loss)	$ 709	$ (464)
Basic earnings (loss) per share	$ 0.08	$ (0.05)
Diluted earnings (loss) per share	$ 0.08	$ (0.05)
Weighted-average basic shares	8,959	8,876
Weighted-average diluted shares	9,080	8,876

See notes to consolidated financial statements

DATA I/O CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

For the three months ended March 31, (in thousands)	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income (loss)	$ 709	$ (464)
Adjustments to reconcile income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	290	272
Gain on sale of assets	(3)	(1)
Equipment transferred to cost of goods sold	158	21
Share-based compensation	75	94
Net change in:		
Trade accounts receivable	(1,591)	2,339
Inventories	161	129
Other current assets	84	103
Accrued cost of business restructuring	(25)	(285)
Accounts payable and accrued liabilities	299	(1,001)
Deferred revenue	316	(119)
Deposits and other long-term assets	(1)	-
Net cash provided by (used in) operating activities	472	1,088
CASH FLOWS FROM INVESTING ACTIVITIES:		
Additions to property, plant and equipment	(368)	(124)
Net proceeds from sale of assets	3	1
Cash provided by (used in) investing activities	(365)	(123)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from issuance of common stock	15	9
Payment of capital lease obligation	(32)	(29)
Cash provided by (used in) financing activities	(17)	(20)
Increase (decrease) in cash and cash equivalents	90	945
Effects of exchange rate changes on cash	(48)	191
Cash and cash equivalents at beginning of year	15,642	13,304
Cash and cash equivalents at end of year	$ 15,684	$ 14,440

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 March 31, 2010 and March 31, 2009 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, 2009 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 months ended March 31, 2010 are not necessarily indicative of the results that may be expected for the year ending December 31, 2010. 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, 2009.

Revenue Recognition

Data I/O recognizes revenue at the time of shipment. When arrangements include multiple elements, we use objective evidence of fair value 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 fair value 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 fair value 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 is 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 in writing by Data I/O.

On those occasions where 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 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 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.

Stock-Based Compensation Expense

Data I/O measures and recognizes compensation expense as required for all share-based payment awards, including employee stock options, stock awards, and employee stock purchases, based on estimated fair values on the grant dates. Total share-based compensation for the three months ended March 31, 2010 and March 31, 2009 was $75,000 and $94,000, 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 months ended March 31, 2010. 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 $81,000 of unrecognized tax benefits related to uncertain tax positions as of March 31, 2010.

Tax years that remain open for examination include 2006, 2007, 2008 and 2009 in the United States of America. In addition, tax years from 1999 to 2005 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 February 2010, the Financial Accounting Standard Board (FASB) issued ASU No. 2010-09, *Subsequent Events (Topic 855): Amendments to Certain Recognition and Disclosure Requirements* ("ASU 2010-09"), which amends the disclosure guidance with respect to the disclosure of subsequent-events procedures. Specifically, the new guidance exempts SEC filers from disclosing the date through which subsequent events have been evaluated, instead requiring them to evaluate subsequent events through the date the financial statements are issued. The impact of adoption of this standard had no financial effect on the accompanying condensed consolidated financial statements.

In January 2010, theFASB issued ASU No. 2010-06, *Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements* ("ASU 2010-06"), which amends the disclosure guidance with respect to fair value measurements. Specifically, the new guidance requires disclosure of amounts transferred in and out of Levels 1 and 2 fair value measurements, a reconciliation presented on a gross basis rather than a net basis of activity in Level 3 fair value measurements, greater disaggregation of the assets and liabilities for which fair value measurements are presented and more robust disclosure of the valuation techniques and inputs used to measure Level 2 and 3 fair value measurements. ASU 2010-06 is effective for interim and annual reporting periods beginning after December 15, 2009, with the exception of the new guidance around the Level 3 activity reconciliations, which is effective for fiscal years beginning after December 15, 2010. The impact of adoption of this standard had no financial effect on the accompanying condensed consolidated financial statements.

In October 2009, an update was made by FASB to revenue arrangements with multiple deliverables. It provides amendments to 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 will be effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. Early adoption is permitted. We are currently assessing the potential impact that adoption of this standard may have on our consolidated financial statements.

In October 2009, an update was made by the FASB to software revenue recognition. 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. This standard requires that hardware components of a tangible product containing software components always be excluded from 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 will be effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. Early adoption is permitted. 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. We are currently assessing the potential impact that adoption of this standard may have on our consolidated financial statements.

NOTE 2 - RECLASSIFICATIONS

Certain prior period balances may have been reclassified to conform to the presentation used in the current period.

NOTE 3 - INVENTORIES

Inventories consisted of the following components (in thousands):

		March 31, 2010		December 31, 2009
(in thousands)				
Raw material	$	2,023	$	2,007
Work-in-process		896		979
Finished goods		826		961
Inventories	$	3,745	$	3,947

NOTE 4   PROPERTY AND EQUIPMENT, NET

Property and equipment consisted of the following components:

		March 31, 2010		December 31, 2009
(in thousands)				
Leasehold improvements	$	394	$	393
Equipment		8,143		8,184
		8,537		8,577
Less accumulated depreciation		6,796		6,758
Property and equipment - net	$	1,741	$	1,819

NOTE 5   BUSINESS RESTRUCTURING

We took 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 March 31, 2010, $133,000 remains accrued and will be fully paid out during 2010 and 2011.

An analysis of the restructuring is as follows:

Downsizing US operations (in thousands)	Reserve Balance 12/31/2008	2009 Expense	2009 Payments/ Write-Offs	Reserve Balance 12/31/2009	2010 Expense	2010 Payments/ Write-Offs	Reserve Balance 3/31/2010
Employee severance	$ 80	$ 34	$ 114	$ -	$ -	$ -	$ -
Facility & other costs	7	208	57	158	-	25	133
Downsizing foreign operations:							
Employee severance	289	(67)	222	-	-	-	-
Facility & other costs	13	28	41	-	-	&	