ACCURAY INC
Form 10-Q
November 05, 2015
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2015

or

o 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: 001-33301

ACCURAY INCORPORATED

(Exact Name of Registrant as Specified in Its Charter)

Delaware	**20-8370041**
(State or Other Jurisdiction of Incorporation or Organization)	(IRS Employer Identification Number)

1310 Chesapeake Terrace

Sunnyvale, California 94089

(Address of Principal Executive Offices Including Zip Code)

(408) 716-4600

(Registrant s Telephone Number, Including Area Code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file reports), and (2) has been subject to such filing requirements for the past 90 days. x Yes o 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 (§ 229.405 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 o

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 definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

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

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

As of October 28, 2015, there were 79,869,955 shares of the Registrant s Common Stock, par value $0.001 per share, outstanding.

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Accuray Incorporated

Form 10-Q for the Quarter Ended September 30, 2015

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PART I. FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

Accuray Incorporated

Condensed Consolidated Balance Sheets

(in thousands, except share amounts and par value)

(Unaudited)

		September 30, 2015		June 30, 2015 (1)
Assets				
Current assets:				
Cash and cash equivalents	$	85,584	$	79,551
Short-term investments		67,513		64,306
Restricted cash		3,795		3,734
Accounts receivable, net of allowance for doubtful accounts of $745 and $709 as of September 30, 2015 and June 30, 2015, respectively		56,636		77,727
Inventories		113,798		106,151
Prepaid expenses and other current assets		16,527		15,991
Deferred cost of revenue		6,799		6,869
Total current assets		350,652		354,329
Property and equipment, net		29,482		31,829
Goodwill		57,965		58,054
Intangible assets, net		13,576		15,564
Deferred cost of revenue		2,264		1,500
Other assets		7,863		8,695
Total assets	$	461,802	$	469,971
Liabilities and stockholders equity				
Current liabilities:				
Accounts payable	$	13,652	$	13,096
Accrued compensation		18,377		21,934
Other accrued liabilities		22,503		18,720
Short-term debt		95,134		
Customer advances		22,949		19,385
Deferred revenue		90,719		96,780
Total current liabilities		263,334		169,915
Long-term liabilities:				
Long-term other liabilities		10,761		10,934
Deferred revenue		13,938		10,489
Long-term debt		109,639		202,853
Total liabilities		397,672		394,191
Commitment and contingencies (Note 5)				
Stockholders Equity:				

Preferred stock, $0.001 par value; authorized: 5,000,000 shares; no shares issued and outstanding				
Common stock, $0.001 par value; authorized: 200,000,000 shares as of September 30, 2015 and June 30, 2015 respectively; issued and outstanding: 79,864,804 and 79,477,838 shares at September 30, 2015 and June 30, 2015, respectively		80		79
Additional paid-in capital		473,025		471,430
Accumulated other comprehensive loss		(646)		(426)
Accumulated deficit		(408,329)		(395,303)
Total stockholders equity		64,130		75,780
Total liabilities and stockholders equity	$	461,802	$	469,971

(1) The condensed consolidated balance sheet at June 30, 2015 has been derived from audited consolidated financial statements.

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

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Accuray Incorporated

Condensed Consolidated Statements of Operations and Comprehensive Loss

(in thousands, except per share amounts)

(Unaudited)

	Three Months Ended September 30, 2015	Three Months Ended September 30, 2014
Net revenue:		
Products	$ 39,995	$ 33,015
Services	49,636	49,366
Total net revenue	89,631	82,381
Cost of revenue:		
Cost of products	23,017	20,665
Cost of services	32,716	33,915
Total cost of revenue	55,733	54,580
Gross profit	33,898	27,801
Operating expenses:		
Research and development	14,296	14,149
Selling and marketing	13,417	17,974
General and administrative	13,416	10,950
Total operating expenses	41,129	43,073
Loss from operations	(7,231)	(15,272)
Other expense, net	(5,091)	(5,461)
Loss before provision for income taxes	(12,322)	(20,733)
Provision for income taxes	704	917
Net loss	$ (13,026)	$ (21,650)
Net loss per share basic and diluted	$ (0.16)	$ (0.28)
Weighted average common shares used in computing loss per share		
Basic and diluted	79,760	77,290
Net loss	$ (13,026)	$ (21,650)
Foreign currency translation adjustment	(258)	(442)
Unrealized gain (loss) on investments, net of tax	38	(141)
Comprehensive loss	$ (13,246)	$ (22,233)

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

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Accuray Incorporated

Condensed Consolidated Statements of Cash Flows

(in thousands)

(Unaudited)

	Three Months Ended September 30, 2015	2014
Cash Flows From Operating Activities		
Net loss	$ (13,026)	$ (21,650)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	4,559	4,978
Share-based compensation	2,514	3,273
Amortization of debt issuance costs	403	363
Amortization and accretion of discount and premium on investments	270	266
Accretion of interest on debt	1,920	1,759
Recovery of (provision for) bad debt, net	36	(127)
Provision for write-down of inventories	424	259
Loss on disposal of property and equipment	8	
Changes in assets and liabilities:		
Accounts receivable	20,902	17,726
Inventories	(7,193)	(13,147)
Prepaid expenses and other assets	(65)	3,233
Deferred cost of revenue	(704)	1,468
Accounts payable	710	9
Accrued liabilities	(13)	(13,237)
Customer advances	3,609	751
Deferred revenue	(2,098)	(643)
Net cash provided by (used in) operating activities	12,256	(14,719)
Cash Flows From Investing Activities		
Purchases of property and equipment, net	(1,544)	(2,691)
Purchases of investments	(15,439)	(45,739)
Sales and maturities of investments	12,000	79,470
Net cash (used in) provided by investing activities	(4,983)	31,040
Cash Flows From Financing Activities		
Proceeds from employee stock plans	1,034	1,886
Taxes paid related to net share settlement of equity awards	(1,060)	
Net cash (used in) provided by financing activities	(26)	1,886
Effect of exchange rate changes on cash and cash equivalents	(1,214)	(3,258)
Net increase in cash and cash equivalents	6,033	14,949
Cash and cash equivalents at beginning of period	79,551	92,346
Cash and cash equivalents at end of period	$ 85,584	$ 107,295

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

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Accuray Incorporated

Notes to Condensed Consolidated Financial Statements

(Unaudited)

1. Summary of Significant Accounting Policies

Description of Business

Accuray Incorporated (together with its subsidiaries, the Company or Accuray) is incorporated in Delaware. The Company designs, develops and sells advanced radiosurgery and radiation therapy systems for the treatment of tumors throughout the body. The Company conducts its business worldwide. The Company has its headquarters in Sunnyvale, California, with additional locations worldwide.

Basis of Presentation and Principles of Consolidation

The condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All significant inter-company transactions and balances have been eliminated in consolidation.

The accompanying condensed consolidated financial statements have been prepared in accordance with United States generally accepted accounting principles (GAAP), pursuant to the rules and regulations of the Securities and Exchange Commission (the SEC). Certain information and note disclosures have been condensed or omitted pursuant to such rules and regulations. The unaudited condensed consolidated financial statements have been prepared on the same basis as the annual financial statements and, in the opinion of management, reflect all adjustments, which include only normal recurring adjustments, necessary for a fair presentation of the periods presented. The results for the three months ended September 30, 2015 are not necessarily indicative of the results to be expected for the year ending June 30, 2016, for any other interim period or for any future year.

These condensed consolidated financial statements should be read in conjunction with the Company s audited consolidated financial statements and accompanying notes for the year ended June 30, 2015 included in the Company s Annual Report on Form 10-K filed with the SEC on August 28, 2015. The Company s significant accounting policies are described in Note 2 to those audited consolidated financial statements and there have been no material changes to such policies.

Recent Accounting Standard Update Not Yet Effective

In May 2014, the FASB issued Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers: Topic 606* (ASU 2014-09), to supersede nearly all existing revenue recognition guidance under GAAP. The core principle of ASU 2014-09 is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration that is expected to be received for those goods or services. ASU 2014-09 defines a five step process to achieve this core principle and, in doing so, it is possible more judgment and estimates may be required within the revenue recognition process than required under existing GAAP including identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each separate performance obligation. On July 9, 2015, FASB approved a one-year deferral of the effective period for ASU 2014-09. The standard will be effective for the Company for the first quarter of fiscal 2019, but entities will be permitted to early adopt the standard as of the original effective date, which would be the first quarter of fiscal 2018 for the Company. The Company may adopt either of two methods: (i) retrospective to each prior reporting period presented with the option to elect certain practical expedients as defined within ASU 2014-09; or (ii) retrospective with the cumulative effect of initially applying ASU 2014-09 recognized at the date of initial application and providing certain additional disclosures as defined per ASU 2014-09. The Company has not yet selected a transition method, has not yet determined whether it will select early adoption and is currently evaluating the impact of pending adoption of ASU 2014-09 on its consolidated financial statements and related disclosures.

Use of Estimates

The preparation of condensed consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosures at the date of the financial statements. Key estimates and assumptions made by the Company relate to revenue recognition, assessment of recoverability of goodwill and intangible assets, valuation of inventories, share-based compensation expense, income taxes, allowance for doubtful accounts, loss contingencies and corporate bonus expenses. Actual results could differ materially from those estimates.

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Concentration of Credit and Other Risks

The Company s cash, cash equivalents and investments are deposited with several major financial institutions. At times, deposits in these institutions exceed the amount of insurance provided on such deposits. The Company has not experienced any losses in such accounts and does not believe that it is exposed to any significant risk of loss on these balances.

For the three months ended September 30, 2015, there was one customer that represented 15% of total net revenue. For the three months ended September 30, 2014, there were no customers that represented 10% or more of total net revenue. One customer accounted for 17% and 18% of the Company s total accounts receivable as of September 30, 2015 and June 30, 2015, respectively.

Accounts receivable are typically not collateralized. The Company performs ongoing credit evaluations of its customers and maintains reserves for potential credit losses. Accounts receivable are deemed past due in accordance with the contractual terms of the agreement. Accounts are charged against the allowance for doubtful accounts once collection efforts are unsuccessful.

Single source suppliers presently provide the Company with several components. In most cases, if a supplier was unable to deliver these components, the Company believes that it would be able to find other sources for these components subject to any regulatory qualifications, if required.

Revenue Recognition

The Company earns revenue from the sale of products and related services. The Company records its revenues net of any value added or sales tax. For arrangements with multiple elements, the Company allocates arrangement fees to products and services based upon Vendor Specific Objective Evidence (VSOE) of fair value of the respective elements, Third-Party Evidence (TPE), or Best Estimate of Selling Price (BESP), using the relative selling price method.

Product and Service Revenue

The majority of product revenue is generated from sales of CyberKnife and TomoTherapy systems. If the Company is responsible for installation, the Company recognizes revenue after installation and acceptance of the system. Otherwise, revenue is recognized upon delivery, assuming all other revenue recognition criteria are met.

The Company offers its systems with post-contract customer support (PCS) contracts, installation services, training, and professional services. PCS contracts provide planned and corrective maintenance services, software updates, bug fixes, as well as call-center support. Service revenue is generated primarily from PCS (warranty period services and post warranty services), installation services, training, parts and upgrades that are sold under service contracts, and professional services. PCS revenue is deferred and recognized over the service period. Installation service revenue is recognized concurrent with system revenue. Training and professional service revenues that are not deemed essential to the functionality of the systems are recognized as such services are performed.

Costs associated with service revenue are expensed when incurred, except when those costs are related to parts or system upgrades where revenue recognition has been deferred. In those cases, the costs are deferred and are recognized over the period of revenue recognition.

Net Loss Per Common Share

Basic and diluted net loss per share is computed by dividing net loss attributable to stockholders by the weighted average number of common shares outstanding during the period.

A reconciliation of the numerator and denominator used in the calculation of basic and diluted net loss per share follows (in thousands):

	Three Months Ended September 30,	
	2015	**2014**
Numerator:		
Net loss used in computing net loss per share	$ (13,026)	$ (21,650)
Denominator:		
Weighted average shares used in computing basic and diluted loss per share	79,760	77,290

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The potentially dilutive shares of the Company s common stock resulting from the assumed exercise of outstanding stock options, the vesting of Restricted Stock Units (RSU), Market Stock Units (MSU) and Performance Stock Units (PSU), and the purchase of shares under the Employee Stock Purchase Program (ESPP), as determined under the treasury stock method, are excluded from the computation of diluted net loss per share because their effect would have been anti-dilutive. Additionally, the 3.75% Convertible Senior Notes due August 1, 2016 (the 3.75% Convertible Notes), the 3.50% Convertible Senior Notes due February 1, 2018 (the 3.50% Convertible Notes) and the 3.50% Series A Convertible Notes (the 3.50% Series A Convertible Notes) due February 1, 2018 (together, the Convertible Notes) are included in the calculation of diluted net income per share only if their inclusion is dilutive. For the three months ended September 30, 2015 and 2014, the potentially dilutive shares under the Convertible Notes were excluded from the calculation of diluted net loss per share as their inclusion would have been anti-dilutive. The following table sets forth all potentially dilutive securities excluded from the computation in the table above because their effect would have been anti-dilutive (in thousands):

	As of September 30,	
	2015	**2014**
Stock options	2,458	3,032
RSUs, PSUs and MSUs	4,095	4,024
3.50% Convertible Notes	8,378	8,378
3.50% Series A Convertible Notes		3,352
	14,931	18,786

Outstanding Convertible Notes Diluted Share Impact

The 3.75% Convertible Notes and 3.50% Series A Convertible Notes have an optional physical (share), cash or combination settlement feature and contain certain conditional conversion features. Due to the optional cash settlement feature and management s intent to settle the principal amount thereof in cash, the conversion shares underlying the outstanding principal amount of the 3.75% Convertible Notes and 3.50% Series A Convertible Notes, totaling approximately 10.6 million shares and 13.2 million shares, respectively, were not included in the potentially diluted share count table above. The Company s average stock price did not exceed the conversion price of the 3.75% Convertible Notes as of September 30, 2015 and 2014. The zero and 3.4 million potentially dilutive shares of the 3.50% Series A Convertible Notes as of September 30, 2015 and 2014, respectively, included in the table above represent the premium over the principal amount due to the higher average share price above the conversion price. The number of premium shares included in the Company s diluted share count will vary with fluctuations in the Company s share price. Higher actual share prices result in a greater number of premium shares.

Segment Information

The Company has determined that it operates in only one segment, as it only reports profit and loss information on an aggregate basis to its chief operating decision maker. Revenue by geographic region is based on the shipping addresses of the Company s customers. The following summarizes revenue by geographic region (in thousands):

	Three Months Ended September 30,	
	2015	**2014**
Americas	$ 45,290	$ 38,478
Europe, Middle East, India and Africa	23,034	30,937
Asia-Pacific (excluding Japan and India)	16,982	4,882

Japan		4,325		8,084
Total	$	89,631	$	82,381

Information regarding geographic areas in which the Company has long lived tangible assets is as follows (in thousands):

		September 30, 2015		June 30, 2015
Americas	$	25,980	$	28,182
Europe, Middle East, India and Africa		793		929
Asia-Pacific (excluding Japan and India)		527		455
Japan		2,182		2,263
Total	$	29,482	$	31,829

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2. Balance Sheet Components

Financing receivables

A financing receivable is a contractual right to receive money, on demand or on fixed or determinable dates, that is recognized as an asset in the Company s balance sheet. The Company s financing receivables, consisting of its accounts receivable with contractual maturities of more than one year, totaled $2.0 million and $1.6 million at September 30, 2015 and June 30, 2015, respectively and are included in Other Assets in the consolidated balance sheets. There was no balance in the allowance for doubtful accounts related to such financing receivables as of September 30, 2015 and June 30, 2015, respectively, as revenue is recognized on a cash basis for these receivables.

Inventories

Inventories consisted of the following (in thousands):

		September 30, 2015		June 30, 2015
Raw materials	$	50,336	$	46,356
Work-in-process		17,802		15,445
Finished goods		45,660		44,350
Inventories	$	113,798	$	106,151

Property and equipment, net

Property and equipment, net consisted of the following (in thousands):

		September 30, 2015		June 30, 2015
Furniture and fixtures	$	4,677	$	4,674
Computer and office equipment		12,085		11,808
Software		11,088		10,992
Leasehold improvements		20,898		19,428
Machinery and equipment		48,750		47,031
Construction in progress		4,097		8,273
		101,595		102,206
Less: Accumulated depreciation		(72,113)		(70,377)
Property and equipment, net	$	29,482	$	31,829

Depreciation expense related to property and equipment for the three months ended September 30, 2015 and 2014 was $2.6 million and $3.0 million, respectively.

3. Goodwill and Intangible Assets

Goodwill

Activity related to goodwill consisted of the following (in thousands):

	Three Months Ended September 30, 2015	Year Ended June 30, 2015
Balance at the beginning of the period	$ 58,054	$ 58,091
Currency translation	(89)	(37)
Balance at the end of the period	$ 57,965	$ 58,054

In the second quarter of fiscal 2015, the Company performed its annual goodwill impairment test. Based on this analysis, the Company determined that there was no impairment to goodwill. The Company will continue to monitor its recorded goodwill for indicators of impairment. In the three months ended September 30, 2015, there were no indicators of impairment.

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Intangible Assets

The Company s unamortized intangible assets associated with completed acquisitions at September 30, 2015 and June 30, 2015 are as follows (in thousands):

		September 30, 2015			June 30, 2015		
	Useful Lives (in years)	**Gross Carrying Amount**	**Accumulated Amortization**	**Net Amount**	**Gross Carrying Amount**	**Accumulated Amortization**	**Net Amount**
Developed technology	5 6	$ 46,746	$ (33,170)	$ 13,576	$ 46,700	$ (31,136)	$ 15,564

The Company did not identify any triggering events that would indicate potential impairment of its definite-lived intangible and long-lived assets as of September 30, 2015 and June 30, 2015.

Amortization expense related to intangible assets for the three months ended September 30, 2015 and 2014 was $2.0 million and $2.0 million, respectively.

The estimated future amortization expense of purchased intangible assets as of September 30, 2015 is as follows (in thousands):

Year Ending June 30,	**Amount**
2016 (remaining 9 months)	$ 5,965
2017	7,568
2018	43
	$ 13,576

4. Financial Instruments

The Company considers all highly liquid investments held at major banks, certificates of deposit and other securities with original maturities of three months or less to be cash equivalents.

The Company classifies all of its investments as available-for-sale at the time of purchase because it is management s intent that these investments are available for current operations and includes these investments on its balance sheet as short-term investments. Investments with original maturities longer than three months include commercial paper, U.S. agency securities, non-U.S. government securities and investment-grade corporate debt securities. Investments classified as available-for-sale are recorded at fair market value with the related unrealized gains and losses included in accumulated other comprehensive income (loss), a component of stockholders equity. Realized gains and losses are recorded based on specific identification of each security s cost basis.

The Company defines fair value as the price that would be received to sell an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The fair value hierarchy contains three levels of inputs that may be used to measure fair value, as follows:

Level 1 Unadjusted quoted prices that are available in active markets for the identical assets or liabilities at the measurement date.

Level 2 Other observable inputs available at the measurement date, other than quoted prices included in Level 1, either directly or indirectly, including:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets in non-active markets;
- Inputs other than quoted prices that are observable for the asset or liability; and
- Inputs that are derived principally from or corroborated by other observable market data.

Level 3 Unobservable inputs that cannot be corroborated by observable market data and reflect the use of significant management judgment. These values are generally determined using pricing models for which the assumptions utilize management s estimates of market participant assumptions.

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The following tables summarize the amortized cost, gross unrealized gains, gross unrealized losses and fair value by significant investment category for cash, cash equivalents and short-term investments (in thousands):

	September 30, 2015				
				Estimated Market Value	
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Cash and Cash Equivalents	Short-term Investments
Cash	$ 84,458	$	$	$ 84,458	$
Level 1					