Xtant Medical Holdings, Inc.
Form 10-Q
August 14, 2017

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, 2017

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: 001-34951

XTANT MEDICAL HOLDINGS, INC.

(Exact name of registrant as specified in its charter)

Delaware **20-5313323**

(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

664 CRUISER LANE

BELGRADE, MONTANA 59714

(Address of principal executive offices) (Zip code)

(406) 388-0480

(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 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. (Check one):

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

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ¨

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

Number of shares of common stock, $0.000001 par value, of registrant outstanding at August 14, 2017: 18,092,603.

XTANT MEDICAL HOLDINGS, INC.

FORM 10-Q

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PART I - FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

XTANT MEDICAL HOLDINGS, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

	As of June 30, 2017 (unaudited)	**As of December 31, 2016**
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 1,664,543	$ 2,578,267
Trade accounts receivable, net of allowance for doubtful accounts of $1,923,287 and $1,653,385, respectively	15,847,142	18,991,872
Current inventories, net	24,932,155	26,266,457
Prepaid and other current assets	831,239	1,149,615
Total current assets	43,275,079	48,986,211
Non-current inventories, net	641,124	971,854
Property and equipment, net	14,037,043	15,840,730
Goodwill	41,534,626	41,534,626
Intangible assets, net	33,672,915	35,940,810
Other assets	1,133,331	827,374
Total Assets	$ 134,294,118	$ 144,101,605
LIABILITIES & STOCKHOLDERS’ DEFICIT		
Current Liabilities:		
Accounts payable	$ 8,446,454	$ 10,471,944
Accounts payable - related party (note 13)	291,785	640,442
Revolving line of credit	-	10,448,283
Accrued liabilities	11,627,528	8,982,187
Warrant derivative liability	177,380	333,613
Current portion of capital lease obligations	302,064	244,847
Total current liabilities	20,845,211	31,121,316
Long-term Liabilities:		
Capital lease obligation, less current portion	747,000	832,152

Long-term convertible debt, less issuance costs	70,708,939	68,937,247
Long-term debt, less issuance costs	63,285,428	50,284,187
Total Liabilities	155,586,578	151,174,902
Commitments and Contingencies (note 10)		
Stockholders' Deficit:		
Preferred stock, $0.000001 par value; 5,000,000 shares authorized; no shares issued and Outstanding	-	-
Common stock, $0.000001 par value; 95,000,000 shares authorized; 18,092,603 shares issued and outstanding as of June 30, 2017 and 17,249,315 shares issued and outstanding as of December 31, 2016	18	17
Additional paid-in capital	86,101,803	85,461,210
Accumulated deficit	(107,394,281)	(92,534,524)
Total Stockholders' Deficit	(21,292,460)	(7,073,297)
Total Liabilities & Stockholders' Deficit	$134,294,118	$144,101,605

See notes to unaudited condensed consolidated financial statements.

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XTANT MEDICAL HOLDINGS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

	Three Months Ended June 30,		**Six Months Ended June 30,**	
	2017	**2016**	**2017**	**2016**
Revenue				
Orthopedic product sales	$ 21,371,030	$ 21,311,322	$ 43,367,345	$ 42,119,357
Other revenue	37,130	150,248	123,484	319,548
Total Revenue	21,408,160	21,461,570	43,490,829	42,438,905
Cost of sales	7,880,639	6,758,071	14,438,241	13,635,338
Gross Profit	13,527,521	14,703,499	29,052,588	28,803,567
Operating Expenses				
General and administrative	4,526,543	3,899,280	8,654,811	7,383,992
Sales and marketing	11,137,082	10,420,028	22,134,101	20,932,994
Research and development	640,045	783,897	1,338,680	1,683,472
Depreciation and amortization	1,469,603	1,216,696	2,750,568	2,425,030
Acquisition and integration related expenses	-	450,755	-	752,528
Separation related expenses	380,548	-	604,920	-
Non-cash consulting expense	91,857	55,296	236,580	110,592
Total Operating Expenses	18,245,678	16,825,952	35,719,660	33,288,608
Loss from Operations	(4,718,157)	(2,122,453)	(6,667,072)	(4,485,041)
Other Income (Expense)				
Interest expense	(3,328,262)	(2,984,186)	(6,728,651)	(5,811,361)
Change in warrant derivative liability	(13,798)	477,639	156,233	496,329
Other income (expense)	(1,632,612)	166,425	(1,620,268)	(258,574)
Total Other Income (Expense)	(4,974,672)	(2,340,122)	(8,192,686)	(5,573,606)
Net Loss from Operations	$ (9,692,829)	$ (4,462,575)	$ (14,859,758)	$ (10,058,647)
Net loss per share:				
Basic	$ (0.54)	$ (0.37)	$ (0.82)	$ (0.84)
Dilutive	$ (0.54)	$ (0.37)	$ (0.82)	$ (0.84)
Shares used in the computation:				
Basic	18,092,603	12,101,356	18,012,959	11,999,478
Dilutive	18,092,603	12,101,356	18,012,959	11,999,478

See notes to unaudited condensed consolidated financial statements.

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XTANT MEDICAL HOLDINGS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Six Months Ended June 30,	
	2017	2016
Operating activities:		
Net loss	$(14,859,758)	$(10,058,647)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	4,170,859	3,649,361
Non-cash interest	6,211,365	2,541,890
Loss on disposal of fixed assets	968,591	-
Non-cash consulting expense/stock option expense	397,174	271,374
Provision for losses on accounts receivable and inventory	1,063,331	432,781
Change in derivative warrant liability	(156,233)	(496,329)
Changes in operating assets and liabilities:		
Accounts receivable	2,544,399	207,934
Inventories	1,202,035	(2,673,670)
Prepaid and other assets	12,417	(708,693)
Accounts payable	(2,374,147)	3,652,113
Accrued liabilities	63,235	(4,568,572)
Net cash used in operating activities	(756,732)	(7,750,458)
Investing activities:		
Purchases of property and equipment and intangible assets	(1,067,868)	(4,369,562)
Net cash used in investing activities	(1,067,868)	(4,369,562)
Financing activities:		
Proceeds from long-term debt	11,387,094	-
Payments on capital leases	(27,935)	(49,428)
Proceeds from the issuance of Convertible Debt	-	2,238,166
Proceeds from Revolving Line of Credit	-	5,480,671
Payments on Revolving Line of Credit	(10,448,283)	-
Net proceeds from issuance of stock	-	300,000
Net cash provided by financing activities	910,876	7,969,409
Net change in cash and cash equivalents	(913,724)	(4,150,611)
Cash and cash equivalents at beginning of period	2,578,267	6,368,016
Cash and cash equivalents at end of period	$1,664,543	$2,217,405

See notes to unaudited condensed consolidated financial statements.

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Notes to Unaudited Condensed Consolidated Financial Statements

(1) Business Description and Summary of Significant Accounting Policies

Business Description

The accompanying condensed consolidated financial statements include the accounts of Xtant Medical Holdings, Inc. (“Xtant”), formerly known as Bacterin International Holdings, Inc., a Delaware corporation, and its wholly owned subsidiaries, Xtant Medical, Inc., a Delaware corporation, Bacterin International, Inc., (“Bacterin”) a Nevada corporation and X-Spine Systems, Inc. (“X-spine”), an Ohio corporation, (Xtant Medical, Bacterin and X-spine are jointly referred to herein as the “Company”). All intercompany balances and transactions have been eliminated in consolidation. Xtant develops, manufactures and markets regenerative orthopedic products for domestic and international markets and fixation devices. Xtant products serve the combined specialized needs of orthopedic and neurological surgeons, including orthobiologics for the promotion of bone healing, implants and instrumentation for the treatment of spinal disease, tissue grafts for the treatment of orthopedic disorders to promote healing following spine, cranial and foot surgeries and the development, manufacturing and sale of medical devices for use in orthopedic spinal surgeries.

On July 31, 2015, Xtant acquired all of the outstanding capital stock of X-spine for approximately $60 million in cash, repayment of approximately $13 million of X-spine debt, and 4,242,655 shares of Xtant common stock. Following the closing of the acquisition, on July 31, 2015 Bacterin International Holdings, Inc. changed its name to Xtant Medical Holdings, Inc. On August 6, 2015 Xtant formed a new wholly owned subsidiary, Xtant Medical, Inc., a Delaware corporation to facilitate the integration of Bacterin and X-spine.

The markets in which the Company competes are highly competitive and rapidly changing. Significant technological advances, changes in customer requirements, or the emergence of competitive products with new capabilities or technologies could adversely affect the Company’s operating results. The Company’s business could be harmed by a decline in demand for, or in the prices of, its products or as a result of, among other factors, any change in pricing or distribution methods, increased price competition, changes in government regulations or a failure by the Company to keep up with technological change. Further, a decline in available donors could have an adverse impact on our business.

The accompanying interim condensed consolidated financial statements of Xtant for the three and six months ended June 30, 2017 and 2016 are unaudited and are prepared in accordance with accounting principles generally accepted in the United States of America. They do not include all disclosures required by generally accepted accounting principles for annual consolidated financial statements, but in the opinion of management, include all adjustments, consisting only of normal recurring items, necessary for a fair presentation. Interim results are not necessarily indicative of results which may be achieved in the future for the full year ending December 31, 2017.

These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto which are included in Xtant's Annual Report on Form 10-K for the year ended December 31, 2016. The accounting policies set forth in those annual consolidated financial statements are the same as the accounting policies utilized in the preparation of these condensed consolidated financial statements, except as modified for appropriate interim consolidated financial statement presentation.

Going Concern

The Company has incurred losses since its inception. The terms, conditions and amounts outstanding under the Company's debt agreements (See Note 7, "Debt" below) raise substantial doubt about the Company's ability to continue as a going concern. The Company has established a special committee of its board of directors to evaluate restructuring alternatives assist in related negotiations with the Company's lenders and consider alternatives for raising new capital. The Company also is evaluating various cost-reduction and cash flow improvement measures. However, there can be no assurance that the Company will be successful in these efforts.

The accompanying condensed consolidated financial statements have been prepared assuming that the Company will continue as a going concern; however, the above conditions raise substantial doubt about the Company's ability to do so. The condensed consolidated financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classifications of liabilities that may result should the Company be unable to continue as a going concern.

CRO Agreement

On May 8, 2017, the Company entered into an agreement (the "CRO Agreement") with Aurora Management Partners Inc. ("Aurora"). Pursuant to the CRO Agreement, David Baker serves as Chief Restructuring Officer of the Company (the "CRO") and Wayne Tanner serves as a Deputy Restructuring Officer of the Company. The CRO and Aurora personnel assisting on this engagement report to the special restructuring committee of the board of directors of the Company and provide periodic updates on progress made in fulfilling the scope of services. The term of the agreement will continue until the engagement is completed or earlier if the engagement is terminated by either party. Aurora is paid the hourly rates set forth on Schedule A to the CRO Agreement and is reimbursed for its expenses actually incurred in providing the services. The CRO Agreement may be terminated by either party, in its sole discretion, for any reason and the termination is effective immediately upon the other party's receipt of written notice of the termination.

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Concentrations and Credit Risk

The Company's accounts receivable are due from a variety of health care organizations and distributors throughout the world. No single customer accounted for more than 10% of revenue or accounts receivable for the comparable periods. The Company provides for uncollectible amounts when specific credit issues arise. Management's estimates for uncollectible amounts have been adequate during prior periods, and management believes that all significant credit risks have been identified at June 30, 2017.

In the six months ended June 30, 2017, Xtant purchased from Norwood Medical less than 10% of its operating products (See Note 13, "Related Party Transactions" below) and approximately 14% for the same period in 2016.

Use of Estimates

The preparation of the consolidated financial statements requires management of the Company to make a number of estimates and assumptions relating to the reported amount of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the period. Significant estimates include the carrying amount of property and equipment, goodwill, and intangible assets and liabilities; valuation allowances for trade receivables, inventory, and deferred income tax assets and liabilities; valuation of the warrant derivative liability, inventory, and estimates for the fair value of stock options grants and other equity awards upon which the Company determines stock-based compensation expense. Actual results could differ from those estimates.

Long-Lived Assets

Long-lived assets, including intangible assets, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the estimated fair value of the assets

Goodwill

Goodwill represents the excess of costs over fair value of assets of businesses acquired. Goodwill and intangible assets acquired in a purchase business combination and determined to have indefinite useful lives are not amortized, instead they are tested for impairment at least annually and whenever events or circumstances indicate the carrying amount of such asset may not be recoverable. In its evaluation of goodwill, the Company performs an assessment of qualitative factors to determine if it is more-likely-than-not that goodwill might be impaired and whether it is necessary to perform the two-step goodwill impairment. The Company conducts its annual impairment test on December 31 of each year.

Revenue Recognition

Revenue is recognized when all of the following criteria are met: a) the Company has entered into a legally binding agreement with the customer; b) the products or services have been delivered; c) the Company's fee for providing the products and services is fixed or determinable; and d) collection of the Company's fee is probable.

The Company's policy is to record revenue net of any applicable sales, use, or excise taxes. If an arrangement includes a right of acceptance or a right to cancel, revenue is recognized when acceptance is received or the right to cancel has expired.

The Company ships to certain customers under consignment arrangements whereby the Company's product is stored by the customer. The customer is required to report the use to the Company and upon such notice, the Company invoices the customer and revenue is recognized when above criteria have been met.

Research and Development

Research and development costs, which are principally related to internal costs for the development of new devices and biologics and processes are expensed as incurred.

Other Income (Expense)

Other income (expense) primarily consists of non-recurring items that are outside of the normal Company's operations such as other related legal expenses, gain or loss on the sale of fixed assets, restructuring costs and miscellaneous minor adjustments to account balances.

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Net Loss Per Share

Basic net income (loss) per share is computed by dividing net income (loss) by the weighted average number of common shares outstanding. Shares issued during the period and shares reacquired during the period are weighted for the portion of the period that they were outstanding. Diluted net income (loss) per share is computed in a manner consistent with that of basic earnings per share while giving effect to all potentially dilutive common shares outstanding during the period, which include the assumed exercise of stock options and warrants using the treasury stock method. Diluted net loss per share was the same as basic net loss per share for the six months ended June 30, 2017 and 2016, as shares issuable upon the exercise of stock options and warrants were anti-dilutive as a result of the net losses incurred for those periods. Dilutive earnings per share are not reported as their effects of including 7,477,910 and 1,798,192 outstanding stock options and warrants for the six months ended June 30, 2017 and 2016, respectively, are anti-dilutive.

Fair Value of Financial Instruments

The carrying values of financial instruments, including trade accounts receivable, accounts payable, other accrued expenses and long-term debt, approximate their fair values based on terms and related interest rates.

The Company follows a framework for measuring fair value. The framework provides a hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The three levels of the fair value hierarchy are described below:

Level 1: Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets.

Level 2: Inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

A financial instrument's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. During the six months ended June 30, 2017 and 2016, there was no reclassification in financial assets or liabilities between Level 1, 2 or 3 categories.

The following table sets forth by level, within the fair value hierarchy, our liabilities that are measured at fair value on a recurring basis:

Warrant derivative liability

	As of June 30, 2017	**As of December 31, 2016**
Level 1	-	-
Level 2	-	-
Level 3	$177,380	$ 333,613