Stereotaxis, Inc.
Form 10-Q
November 13, 2018

Table of Contents

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, 2018

[ ] **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: 001-36159

STEREOTAXIS, INC.

(Exact name of registrant as specified in its charter)

Delaware	**94-3120386**
(State of Incorporation)	**(I.R.S. employer identification no.)**
4320 Forest Park Avenue Suite 100 St. Louis, Missouri	**63108**
(Address of principal executive offices)	**(Zip Code)**

Registrant's telephone number, including area code: (314) 678-6100

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Registration S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). [X] Yes [ ] No

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

Large accelerated filer	[ ]	Accelerated filer	[ ]
Non-accelerated filer	[ ]	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 [X] No

The number of outstanding shares of the registrant's common stock on October 31, 2018 was 59,052,782.

Table of Contents

STEREOTAXIS, INC.

INDEX TO FORM 10-Q

ITEM 1. FINANCIAL STATEMENTS

STEREOTAXIS, INC.

BALANCE SHEETS

	September 30, 2018 (Unaudited)	December 31, 2017
Assets		
Current assets:		
Cash and cash equivalents	$11,570,566	$3,686,302
Accounts receivable, net of allowance of $300,510 and $361,350 in 2018 and 2017, respectively	5,088,111	4,287,255
Inventories, net	1,202,457	1,146,971
Prepaid expenses and other current assets	970,397	750,085
Total current assets	18,831,531	9,870,613
Property and equipment, net	452,639	592,688
Intangible assets, net	109,979	159,470
Other assets	226,939	44,432
Total assets	$19,621,088	$10,667,203
Liabilities and stockholders' equity (deficit)		
Current liabilities:		
Accounts payable	$1,574,035	$1,654,101
Accrued liabilities	2,822,958	3,195,247
Deferred revenue	6,365,676	5,702,769
Warrants	-	19,574,977
Total current liabilities	10,762,669	30,127,094
Long-term deferred revenue	502,893	611,863
Other liabilities	621,573	535,369
Total liabilities	11,887,135	31,274,326
Convertible Preferred stock:		
Convertible Preferred stock, par value $0.001; 10,000,000 shares authorized, 23,900 shares outstanding at 2018 and 2017	5,960,475	5,960,475
Stockholders' equity (deficit):		
Common stock, par value $0.001; 300,000,000 shares authorized, 59,044,164 and 22,805,731 shares issued at 2018 and 2017, respectively	59,044	22,806
Additional paid in capital	478,071,950	450,748,403
Treasury stock, 4,015 shares at 2018 and 2017	(205,999)	(205,999)
Accumulated deficit	(476,151,517)	(477,132,808)
Total stockholders' equity (deficit)	1,773,478	(26,567,598)
Total liabilities and stockholders' equity (deficit)	$19,621,088	$10,667,203

See accompanying notes.

STEREOTAXIS, INC.

STATEMENTS OF OPERATIONS

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Revenue:				
Systems	$715,484	$1,597,537	$1,043,510	$3,644,871
Disposables, service and accessories	6,839,995	6,546,198	21,035,002	19,943,562
Total revenue	7,555,479	8,143,735	22,078,512	23,588,433
Cost of revenue:				
Systems	596,869	888,800	1,257,980	2,029,760
Disposables, service and accessories	1,036,589	1,032,569	3,029,875	3,350,480
Total cost of revenue	1,633,458	1,921,369	4,287,855	5,380,240
Gross margin	5,922,021	6,222,366	17,790,657	18,208,193
Operating expenses:				
Research and development	2,000,780	1,619,749	5,995,800	4,976,892
Sales and marketing	2,819,101	3,079,562	9,911,514	10,479,626
General and administrative	1,215,920	1,355,258	3,753,703	4,921,513
Total operating expenses	6,035,801	6,054,569	19,661,017	20,378,031
Operating income (loss)	(113,780)	167,797	(1,870,360)	(2,169,838)
Other income (expense)	-	(4,459,042)	2,590,361	(1,029,479)
Interest expense (net)	(2,515)	(43,077)	(33,271)	(135,336)
Net income (loss)	$(116,295)	$(4,334,322)	$686,730	$(3,334,653)
Cumulative dividend on convertible preferred stock	(361,447)	(337,963)	(1,072,553)	(1,070,812)
Net loss attributable to common stockholders	$(477,742)	$(4,672,285)	$(385,823)	$(4,405,465)
Net loss per share attributable to common stockholders:				
Basic	$(0.01)	$(0.21)	$(0.01)	$(0.20)
Diluted	$(0.01)	$(0.21)	$(0.01)	$(0.20)
Weighted average number of common shares and equivalents:				
Basic	59,008,219	22,750,405	49,733,553	22,551,496
Diluted	59,008,219	22,750,405	49,733,553	22,551,496

Certain prior year amounts have been reclassified to conform to the 2018 presentation.
See accompanying notes.

4

STEREOTAXIS, INC.

STATEMENTS OF CASH FLOWS

(Unaudited)

	Nine Months Ended September 30,	
	2018	2017
Cash flows from operating activities		
Net income (loss)	$686,730	$(3,334,653)
Adjustments to reconcile net income to cash used in operating activities:		
Depreciation	394,154	412,793
Amortization of intangibles	49,491	149,491
Amortization of deferred finance costs	24,657	74,793
Share-based compensation	465,851	625,854
Loss on asset disposal	1,449	20,772
Adjustment of warrants	(2,590,361)	1,029,479
Changes in operating assets and liabilities:		
Accounts receivable	(800,856)	617,873
Inventories	(55,486)	775,577
Prepaid expenses and other current assets	(131,116)	(46,427)
Other assets	(1,799)	(7,105)
Accounts payable	(80,066)	(889,868)
Accrued liabilities	(372,289)	(979,526)
Deferred revenue	553,937	(2,497,775)
Other liabilities	86,204	176,905
Net cash used in operating activities	(1,769,500)	(3,871,817)
Cash flows from investing activities		
Purchase of fixed assets	(255,554)	(72,082)
Net cash used in investing activities	(255,554)	(72,082)
Cash flows from financing activities		
Payments of deferred financing costs	-	(100,000)
Proceeds from issuance of stock, net of issuance costs	44,621	29,573
Proceeds from warrant exercise	9,864,697	-
Net cash provided by (used in) financing activities	9,909,318	(70,427)
Net increase (decrease) in cash and cash equivalents	7,884,264	(4,014,326)
Cash and cash equivalents at beginning of period	3,686,302	8,501,392
Cash and cash equivalents at end of period	$11,570,566	$4,487,066

See accompanying notes.

STEREOTAXIS, INC.

NOTES TO FINANCIAL STATEMENTS

(Unaudited)

Notes to Financial Statements

In this report, “Stereotaxis”, the “Company”, “Registrant”, “we”, “us”, and “our” refer to Stereotaxis, Inc. and its wholly owned subsidiaries. Epoch®, Niobe®, Odyssey®, Odyssey Cinema™, Vdrive®, Vdrive Duo™, V-CAS™, V-Loop™, V-Sono™, V-CAS Deflect™, QuikCAS™, and Cardiodrive® are trademarks of Stereotaxis, Inc. All other trademarks that appear in this report are the property of their respective owners.

1. Description of Business

Stereotaxis designs, manufactures and markets the *Epoch* Solution, which is an advanced remote robotic navigation system for use in a hospital’s interventional surgical suite, or “interventional lab”, that we believe revolutionizes the treatment of arrhythmias and coronary artery disease by enabling enhanced safety, efficiency, and efficacy for catheter-based, or interventional, procedures. The *Epoch* Solution is comprised of the *Niobe* ES Remote Magnetic Navigation System (“*Niobe* ES system”), *Odyssey* Information Management Solution (“*Odyssey* Solution”), and the *Vdrive* Robotic Navigation System (“*Vdrive* system”), and related devices.

The *Niobe* system is designed to enable physicians to complete more complex interventional procedures by providing image-guided delivery of catheters and guidewires through the blood vessels and chambers of the heart to treatment sites. This is achieved using externally applied magnetic fields that govern the motion of the working tip of the catheter or guidewire, resulting in improved navigation, efficient procedures, and reduced x-ray exposure. As of September 30, 2018, the Company had an installed base of 127 *Niobe* ES systems.

In addition to the *Niobe* system and its components, Stereotaxis also has developed the *Odyssey* Solution, which consolidates all lab information enabling doctors to focus on the patient for optimal procedure efficiency. The system also features a remote viewing and recording capability called *Odyssey Cinema*, which is an innovative solution delivering synchronized content for optimized workflow, advanced care, and improved productivity. This tool includes an archiving capability that allows clinicians to store and replay entire procedures or segments of procedures. This information can be accessed from locations throughout the hospital local area network and over the global *Odyssey* Network providing physicians with a tool for clinical collaboration, remote consultation, and training.

Our *Vdrive* system provides navigation and stability for diagnostic and therapeutic devices designed to improve interventional procedures. The *Vdrive* system complements the *Niobe* ES system control of therapeutic catheters for fully remote procedures and enables single-operator workflow and is sold as two options, the *Vdrive* system and the *Vdrive Duo* system. In addition to the *Vdrive* system and the *Vdrive Duo* system, we also manufacture and market various disposable components which can be manipulated by these systems.

We promote the full *Epoch* Solution in a typical hospital implementation, subject to regulatory approvals or clearances. The full *Epoch* Solution implementation requires a hospital to agree to an upfront capital payment and recurring payments. The upfront capital payment typically includes equipment and installation charges. The recurring payments typically include disposable costs for each procedure, equipment service costs beyond warranty period, and software licenses. In hospitals where the full *Epoch* Solution has not been implemented, equipment upgrade or expansion can be implemented upon purchasing of the necessary upgrade or expansion.

The core components of Stereotaxis systems, such as the *Niobe System, Odyssey Workstation, Cardiodrive,* and various disposable interventional devices have received regulatory clearance in the U.S., Europe, Canada, China, Japan and various other countries. We have received the regulatory clearance, licensing and/or CE Mark approvals that allow us to market the *Vdrive* and *Vdrive Duo* systems with the *V-CAS*, *V-Loop* and *V-Sono* devices in the U.S., Canada and European Union. *The V-CAS Deflect* catheter advancement system has been CE Marked for sale in the European Union.

We have successfully integrated our *Niobe* system with digital fluoroscopy systems to provide advanced interventional lab visualization and instrument control through user-friendly computerized interfaces. The maintenance of these arrangements, or the establishment of equivalent alternatives, is critical to our commercialization efforts. The commercial availability of both currently compatible digital imaging fluoroscopy systems is unlikely to continue for multiple years and efforts are being made to ensure the availability of integrated next generation systems and/or equivalent alternatives; however, we cannot provide assurance as to the timeline of the ongoing availability of such compatible systems or our ability to obtain equivalent alternatives on competitive terms or at all.

2. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited financial statements of Stereotaxis, Inc. have been prepared in accordance with generally accepted accounting principles for interim financial information and the instructions to Form 10-Q. Accordingly, they do not include all the disclosures required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, they include all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of the results for the interim periods presented. Operating results for the nine month period ended September 30, 2018 are not necessarily indicative of the results that may be expected for the year ended December 31, 2018 or for future operating periods.

These interim financial statements and the related notes should be read in conjunction with the annual financial statements and notes included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2017 as filed with the Securities and Exchange Commission (SEC) on March 20, 2018.

Going Concern, Liquidity and Management's Plan

The Company believes the cash on hand at September 30, 2018 will be sufficient to meet its obligations as they become due in the ordinary course of business for at least 12 months following the date these financial statements are issued. The Company has sustained operating losses throughout its corporate history and expects that its 2018 expenses will exceed its 2018 gross margin. The Company expects to continue to incur operating losses and negative cash flows until revenues reach a level sufficient to support ongoing operations or expense reductions are in place. The Company's liquidity needs will be largely determined by the success of clinical adoption within the installed base of *Niobe* systems as well as by new placements of capital systems.

Financial Instruments

Financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable, and debt. The carrying value of such amounts reported at the applicable balance sheet dates approximates fair value.

The Company measures certain financial assets and liabilities at fair value on a recurring basis. General accounting principles for fair value measurement established a fair value 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 and liabilities ("Level 1") and the lowest priority to unobservable inputs ("Level 3"). See Note 10 for additional details.

Revenue and Costs of Revenue

The Company adopted ASC 606, Revenue from Contracts with Customers, on January 1, 2018 using the modified retrospective method. As part of the Company's adoption of ASC 606, the Company elected to use the following practical expedients (i) applying the modified retrospective method only to open contracts as of December 31, 2017; (ii) not to adjust the promised amount of consideration for the effects of a significant financing component when the Company expects, at contract inception, that the period between the Company's transfer of a promised product or service to a customer and when the customer pays for that product or service will be one year or less; (iii) to expense costs as incurred for costs to obtain a contract when the amortization period would have been one year or less; and (iv) not to assess whether promised goods or services are performance obligations if they are immaterial in the context of the contract with the customer.

Upon adoption of the new revenue guidance, the Company recorded a cumulative-effect reduction to accumulated deficit of $0.3 million on January 1, 2018 relating primarily to the deferral of previously expensed costs to obtain a contract. The Company capitalized sales commissions paid in connection with multi-year service contracts and is amortizing such asset over the economic life of those contracts. Previously, sales commissions on multi-year service contracts were expensed as incurred. The impact of this change on operating expenses in any given period will depend, in part, on the amount of such commissions incurred and capitalized in relation to the amount of ongoing amortization expense. For the nine months ended September 30, 2018, the Company recorded less than $0.1 million in additional commission expense as a result of adopting the new standard. The Company did not otherwise experience significant changes in the timing or method of revenue recognition for any of its material revenue streams.

We generate revenue from initial capital sales of systems as well as recurring revenue from the sale of our proprietary disposable devices, from royalties paid to the Company on the sale by Biosense Webster of co-developed catheters, and from other recurring revenue including ongoing license and service contracts.

We account for a contract with a customer when there is a legally enforceable contract between the Company and the customer, the rights of the parties are identified, the contract has commercial substance, and collectability of the contract consideration is probable. We record our revenue based on consideration specified in the contract with each customer, net of any taxes collected from customers that are remitted to government authorities.

For contracts containing multiple products and services the Company accounts for individual products and services as separate performance obligations if they are distinct, which is if a product or service is separately identifiable from other items in the bundled package, and if a customer can benefit from it on its own or with other resources that are readily available to the customer. The Company recognizes revenues as the performance obligations are satisfied by transferring control of the product or service to a customer.

For multiple-element arrangements, revenue is allocated to each performance obligation based on its relative standalone selling price. Standalone selling prices are based on observable prices at which the Company separately sells the products or services. If a standalone selling price is not directly observable, then the Company estimates the standalone selling price considering market conditions and entity-specific factors including, but not limited to, features and functionality of the products and services and market conditions. The Company regularly reviews standalone selling prices and updates these estimates as necessary.

Systems:

Contracts related to the sale of systems typically contain separate obligations for the delivery of system(s), installation and an implied obligation to provide software enhancements if and when available for one year following installation. Revenue is recognized when the Company transfers control to the customer, which is generally at the point when acceptance occurs that indicates customer acknowledgment of delivery or installation, depending on the terms of the arrangement. Revenue from the implied obligation to deliver software enhancements if and when available is recognized ratably over the first year following installation of the system as the customer receives the right to software updates throughout the period and is included in Other Recurring Revenue. The Company's system contracts generally do not provide a right of return. Systems are generally covered by a one-year assurance type warranty; warranty costs were not material for the periods presented. Revenue from system delivery and installation represented 5% and 15% of revenue for the nine months ended September 30, 2018 and 2017, respectively.

Disposables:

Revenue from sales of disposable products is recognized when control is transferred to the customers, which generally occurs at the time of shipment, but can also occur at the time of delivery depending on the customer arrangement. Disposable products are covered by an assurance type warranty that provides for the return of defective products. Warranty costs were not material for the periods presented. Disposable revenue represented 33% and 32% of revenue for the nine months ended September 30, 2018 and 2017, respectively.

Royalty:

The Company is entitled to royalty payments from Biosense Webster, payable quarterly based on net revenues from sales of the co-developed catheters. Royalty revenue from the co-developed catheters represented 10% and 9% of revenue for the nine months ended September 30, 2018 and 2017.

Other Recurring Revenue:

Other recurring revenue includes revenue from product maintenance plans, other post warranty maintenance, and the implied obligation to provide software enhancements if and when available for one year following installation. Revenue from services and software enhancements is deferred and amortized over the service or update period, which is typically one year. Revenue related to services performed on a time-and-materials basis is recognized when performed. Other recurring revenue represented 52% and 44% of revenue for the nine months ended September 30, 2018 and 2017, respectively.

	Three months ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Systems	$715,484	$1,597,537	$1,043,510	$3,644,871
Disposables, service and accessories	6,839,995	6,546,198	21,035,002	19,943,562
Total revenue	$7,555,479	$8,143,735	$22,078,512	$23,588,433

Transaction price allocated to remaining performance obligations relates to amounts allocated to products and services for which the revenue has not yet been recognized. A significant portion of this amount relates to the Company's systems contracts and obligations that will be recognized as revenue in future periods. These obligations are generally satisfied within two years after contract inception but may occasionally extend longer. Transaction price representing revenue to be earned on remaining performance obligations on system contracts was approximately $1.0 million as of

September 30, 2018. Performance obligations arising from contracts for disposables, royalty and service are generally expected to be satisfied within one year after entering into the contract.

The following information summarizes the Company's contract assets and liabilities:

	September 30, 2018	December 31, 2017
Contract Assets - Unbilled Receivables	$139,973	$2,917
Product shipped, revenue deferred	661,402	941,724
Deferred service and license fees	6,207,167	5,372,908
Total deferred revenue	6,868,569	6,314,632
Less: Long-term deferred revenue	(502,893)	(611,863)
Total current deferred revenue	$6,365,676	$5,702,769

The Company invoices its customers based on the billing schedules in its sales arrangements. Contract assets primarily represent the difference between the revenue that was earned but not billed on service contracts and revenue from system contracts that was recognized based on the relative selling price of the related performance obligations and the contractual billing terms in the arrangements. Deferred revenue is primarily related to service contracts, for which the service fees are billed up-front, generally quarterly or annually, and for amounts billed in advance for system contracts for which some performance obligations remain outstanding. For service contracts, the associated deferred revenue is generally recognized ratably over the service period. For system contracts, the associated deferred revenue is recognized when the remaining performance obligations are satisfied. The Company did not have any impairment losses on its contract assets for the periods presented.

Revenue recognized for the nine months ended September 30, 2018 and 2017, that was included in the deferred revenue balance at the beginning of each reporting period was $5,125,372 and $7,652,148, respectively.

Assets Recognized from the Costs to Obtain a Contract with a Customer

The Company has determined that sales incentive programs for the Company's sales team meet the requirements to be capitalized as the Company expects to generate future economic benefits from the related revenue generating contracts after the initial capital sales transaction. The costs capitalized as contract acquisition costs included in prepaid expenses and other assets, in the Company's balance sheet was $0.3 million as of September 30, 2018. The Company did not incur any impairment losses during any of the periods presented.

Costs of systems revenue include direct product costs, installation labor and other costs, estimated warranty costs, and initial training and product maintenance costs. These costs are recorded at the time of sale. Costs of disposable revenue include direct product costs and estimated warranty costs and are recorded at the time of sale. Cost of revenue from services and license fees are recorded when incurred.

Share-Based Compensation

The Company accounts for its grants of stock options, stock appreciation rights, restricted shares, and restricted stock units and for its employee stock purchase plan in accordance with the provisions of general accounting principles for share-based payments. These accounting principles require the determination of the fair value of the share-based compensation at the grant date and the recognition of the related expense over the period in which the share-based compensation vests.

The Company utilizes the Black-Scholes valuation model to determine the fair value of stock options and stock appreciation rights at the date of grant. The resulting compensation expense is recognized over the requisite service period, which is generally four years. Restricted shares granted to employees are valued at the fair market value at the date of grant. The Company amortizes the fair market value to expense over the service period. If the shares are subject to performance objectives, the resulting compensation expense is amortized over the anticipated vesting period and is subject to adjustment based on the actual achievement of objectives.

Net Income (Loss) per Common Share ("EPS")

Basic net income (loss) per share is computed by dividing net income (loss) attributable to common shareholders by the number of common shares outstanding during the period. In periods where there is net income, we apply the two-class method to calculate basic and diluted net income (loss) per share of common stock, as our Convertible Preferred Stock is a participating security. The two-class method is an earnings allocation formula that treats a participating security as having rights to earnings that otherwise would have been available to common stockholders. In periods where there is a net loss, the two-class method of computing earnings per share does not apply as our Convertible Preferred Stock does not contractually participate in our losses. We compute diluted net income (loss) per common share using net income (loss) as the "control number" in determining whether potential common shares are dilutive, after giving consideration to all potentially dilutive common shares, including stock options, warrants, unvested restricted stock units outstanding during the period and potential issuance of stock upon the conversion of our Convertible Preferred Stock issued and outstanding during the period, except where the effect of such securities would be antidilutive.

The following table sets forth the computation of basic and diluted EPS:

	Three months ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Net income (loss)	$(116,295)	$(4,334,322)	$686,730	$(3,334,653)
Cumulative dividend on convertible preferred stock	(361,447)	(337,963)	(1,072,553)	(1,070,812)
Net loss attributable to common stockholders	$(477,742)	$(4,672,285)	$(385,823)	$(4,405,465)
Weighted average number of common shares and equivalents:	59,008,219	22,750,405	49,733,553	22,551,496