ARRHYTHMIA RESEARCH TECHNOLOGY INC /DE/
Form 10-Q
July 01, 2013

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 March 31, 2013 or

[ ] Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from ______ to ______

001-9731
(Commission file No.)

ARRHYTHMIA RESEARCH TECHNOLOGY, INC.
(Exact name of registrant as specified in its charter)

DELAWARE	72-0925679
(State or other jurisdiction of incorporation or organization)	(I.R.S. employer identification no.)

25 Sawyer Passway
Fitchburg, Massachusetts 01420
(Address of principal executive offices)

(978) 345-5000
(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 [ ]   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

As of June 28, 2013 there were 2,704,239 shares of the Company's common stock outstanding.

ARRHYTHMIA RESEARCH TECHNOLOGY, INC.

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ARRHYTHMIA RESEARCH TECHNOLOGY, INC. AND SUBSIDIARIES
Consolidated Balance Sheets

	March 31, 2013 (Unaudited)	December 31, 2012 (Audited)
Assets		
Current assets:		
Cash and cash equivalents	$319,991	$477,708
Trade and other accounts receivable, net of allowance for doubtful accounts of $117,098	3,156,881	3,181,721
Inventories, net	2,759,653	2,415,104
Deferred income taxes	199,432	199,432
Income tax receivable	194,912	194,912
Deposits, prepaid expenses and other current assets	452,608	574,999
Current assets from discontinued operations	22,730	34,301
Total current assets	7,106,207	7,078,177
Property, plant and equipment, net	7,136,018	7,158,512
Other intangible assets, net	187,119	156,091
Long-term deferred tax asset, net	2,153,046	2,068,538
Other non-current assets	256,517	214,596
Non-current assets from discontinued operations	246,735	284,300
Total assets	$17,085,642	$16,960,214
Liabilities and Shareholders' Equity		
Current liabilities:		
Demand line of credit	$800,000	$800,000
Current portion of equipment notes	1,093,526	267,043
Accounts payable	2,412,837	2,437,778
Accrued expenses	653,054	393,913
Customer deposits	10,731	121,779
Deferred revenue	307,232	315,268
Performance guarantee liability	1,000,000	1,000,000
Current liabilities from discontinued operations	579,835	600,571
Total current liabilities	6,857,215	5,936,352
Long-term liabilities:		
Long-term equipment note, net of current portion	209,389	991,213
Long-term portion of deferred gain on lease	7,817	8,934
Long-term deferred revenue	305,913	326,982
Total long-term liabilities	523,119	1,327,129
Total liabilities	7,380,334	7,263,481
Shareholders’ equity:		
Preferred stock, $1 par value; 2,000,000 shares authorized, none issued	—	—
Common stock, $0.01 par value; 10,000,000 shares authorized,	39,265	39,265

3,926,491 shares issued, 2,704,239 shares outstanding		
Additional paid-in-capital	11,124,821	11,110,575
Common stock held in treasury, 1,222,252 shares at cost	(3,335,268)	(3,335,268)
Accumulated other comprehensive income from foreign currency translation	42,502	42,502
Retained earnings	1,833,988	1,839,659
Total shareholders' equity	9,705,308	9,696,733
Total liabilities and shareholders' equity	$17,085,642	$16,960,214

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

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ARRHYTHMIA RESEARCH TECHNOLOGY, INC. AND SUBSIDIARIES

Consolidated Statements of Operations

(Unaudited)

	Three months ended March 31, 2013	2012 Revised
Net revenues	$ 5,643,189	$ 5,831,622
Cost of sales	4,691,041	4,521,561
Gross profit	952,148	1,310,061
Selling and marketing	240,375	238,590
General and administrative	724,130	692,659
Research and development	59,402	133,409
Total operating expenses	1,023,907	1,064,658
(Loss) income from operations	(71,759)	245,403
Other (expense), net	(10,683)	(7,625)
(Loss) income from continuing operations before income tax benefit	(82,442)	237,778
Income tax benefit	(84,509)	(96,340)
Income from continuing operations	2,067	334,118
Discontinued Operations:		
Loss from discontinued operations, net of tax benefit of $5,031 and $207,000, respectively	(7,738)	(770,037)
Net loss	$ (5,671)	$ (435,919)
(Loss) income per share - basic and diluted		
Continuing operations	$ 0.00	$ 0.12
Discontinued operations	0.00	(0.28)
Loss per share - basic and diluted	$ 0.00	$ (0.16)
Weighted average common shares outstanding - basic and diluted	2,704,239	2,790,514

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

ARRHYTHMIA RESEARCH TECHNOLOGY, INC. AND SUBSIDIARIES

Consolidated Statement of Changes in Shareholders' Equity

(Unaudited)

	Common Stock		Additional paid-in capital	Treasury stock		Accumulated other comprehensive income	Retained earnings	Total
	Shares	Amount		Shares	Amount			
December 31, 2012	3,926,491	$39,265	$11,110,575	1,222,252	$(3,335,268)	$ 42,502	$1,839,659	$9,696,733
Share-based compensation			14,246					14,246
Net loss							(5,671)	(5,671)
March 31, 2013	3,926,491	$39,265	$11,124,821	1,222,252	$(3,335,268)	$ 42,502	$1,833,988	$9,705,308

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

ARRHYTHMIA RESEARCH TECHNOLOGY, INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows
(Unaudited)

	Three months ended March 31, 2013	2012 Revised
Cash flows from operating activities:		
Net loss	$(5,671)	$(435,919)
Loss from discontinued operations	7,738	770,037
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Loss on sale of fixed assets	—	6,026
Amortization of the gain on lease	(1,117)	(1,117)
Depreciation and amortization	338,543	349,396
Provision for doubtful accounts	—	15,000
Deferred income taxes	(84,508)	(91,840)
Share-based compensation	14,246	37,520
Changes in operating assets and liabilities:		
Trade accounts receivable	24,840	(851,895)
Inventories	(344,549)	(183,648)
Deposits, prepaid expenses and other assets	122,391	(555,541)
Other non-current assets	(41,921)	(124,198)
Accounts payable	(24,940)	658,726
Accrued expenses and other current liabilities	140,521	72,948
Other non-current liabilities	(21,069)	168,199
Net cash provided by (used in) by operating activities of continuing operations	124,504	(166,306)
Net cash used in operating activities of discontinued operations	(46,178)	(632,745)
Net cash provided by (used in) operating activities	78,326	(799,051)
Cash flows from investing activities:		
Purchases of plant, property and equipment	(63,568)	(97,710)
Proceeds from sale of fixed assets	—	303,885
Cash paid for patents and trademarks	(32,828)	(32,509)
Net cash (used in) provided by investing activities of continuing operations	(96,396)	173,666
Net cash provided by (used in) investing activities of discontinued operations	78,814	(425,898)
Net cash used in investing activities	(17,582)	(252,232)
Cash flows from financing activities:		
Proceeds from equipment note	—	262,960
Principal payments on equipment note	(186,657)	—
Cash dividend paid	—	(84,119)
Net cash (used in) provided by financing activities of continuing operations	(186,657)	178,841
Net cash (used in) provided by financing activities of discontinued operations	(41,183)	—
Net cash (used in) provided by financing activities	(227,840)	178,841
Net decrease in cash and cash equivalents	(167,096)	(872,442)
Cash and cash equivalents at beginning of period	508,590	1,358,223
Cash and cash equivalents at end of period	341,494	485,781
Less cash and cash equivalents of discontinued operations at end of period	(21,503)	(70,824)
Cash and cash equivalents of continuing operations at end of period	$319,991	$414,957

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

Arrhythmia Research Technology, Inc.
Notes to the Consolidated Financial Statements
1. Basis of Presentation
The unaudited interim consolidated financial statements and related notes have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC"). Accordingly, certain information and footnote disclosures normally included in complete financial statements prepared in accordance with U.S. generally accepted accounting principles (GAAP) have been omitted pursuant to such rules and regulations. The accompanying unaudited interim consolidated financial statements and related notes should be read in conjunction with the consolidated financial statements and notes thereto included in the Arrhythmia Research Technology, Inc. ("ART") and subsidiaries (the “Company”) Annual Report on Form 10-K for the year ended December 31, 2012 filed with the SEC on May 31, 2013.
The information presented reflects, in the opinion of the management of the Company, all adjustments necessary for a fair presentation of the financial results for the interim periods presented.
The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Operating results for interim periods are not necessarily indicative of results that may be expected for the entire fiscal year.
Operating matters and liquidity
The Company has experienced net losses, including the discontinued operations of WirelessDx. The Company had borrowings of $800,000 under its line of credit with a bank at March 31, 2013. Borrowings under the line of credit had a maturity date of April 30, 2013, however, the line of credit was paid off on April 4, 2013 and replaced by a new credit facility as outlined below.
On March 29, 2013, the Company entered into a multi-year credit facility with a Massachusetts based bank. The new credit facility includes a revolving line of credit ("revolver") of up to $4.0 million, a commercial term loan of $1.5 million and an equipment line of credit of $1.0 million.
The $4.0 million revolver, which provides for borrowings up to 80% of net eligible receivables and 50% of net eligible raw materials inventory, replaces the previous $3.0 million demand line of credit which was scheduled to expire April 30, 2013. The revolver has a maturity date of June 30, 2015.
The $1.5 million commercial term loan was used to refinance existing Equipment notes and to fund other current liabilities of continuing operations. The term loan has a five year term with a maturity date of March 29, 2018.
The equipment line of credit of $1.0 million is for the purchase of capital equipment. Advances on the equipment line shall not exceed 80% of the invoice amount of the equipment being purchased. The term of the equipment line of credit is six years, maturing on March 29, 2019, inclusive of a one year maximum draw period.
The Company expects that its current and anticipated financial resources, including the new credit facility, are adequate to maintain current and planned operations through March 31, 2014. However, if the Company is not successful in generating sufficient revenues, it may not be able to fund its debt obligations or fund operations beyond March 31, 2014. The Company expects to continue to expand its product offerings and improve sales with new and existing channels. The Company expects to meet its goals in these areas and generate the additional cash needed to fund operations into 2013 and beyond; however, there can be no assurance that the Company will be able to do so. The ability of the Company to realize the carrying value of its assets depends on its ability to successfully execute the Company's long-term business plan.
2. Accounting Policies
Principles of Consolidation
The consolidated financial statements include the accounts of ART and it's wholly owned subsidiary, Micron Products, Inc. ("Micron", and collectively with ART, the "Company"). The Company's Pennsylvania subsidiary RMDDxUSA Corp. and its Prince Edward Island subsidiary RMDDx Corporation, collectively "WirelessDx", discontinued operations in the third quarter of 2012 and are presented herein as discontinued operations. All

intercompany balances and transactions have been eliminated in consolidation.

Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting periods. Actual results could differ from those estimates.

Revenue Recognition

Revenue is recorded when all criteria for revenue recognition have been satisfied, which is generally when goods are shipped to the Company's customers. Product revenue is recognized in the period when persuasive evidence of an arrangement with a customer exists, the products are shipped and title has transferred to the customer, the price is fixed or determined and collection is probable.

The Company defers revenue recognition on the sale of certain molds and tools, as well as certain engineering and validation services, until customer acceptance, including inspection and installation requirements, as defined, are achieved. The Company evaluates revenue arrangements with potential multi-element deliverables to determine if there is more than one unit of accounting. A deliverable constitutes a separate unit of accounting when it has standalone value and there are no customer-negotiated refunds or return rights for the undelivered elements. The selling price for each deliverable is based on vendor-specific objective evidence (“VSOE”) if available, third-party evidence (“TPE”) if VSOE is not available, or best estimate of selling price (“BESP”) if neither VSOE or TPE is available. When possible, revenue is allocated to the elements based on VSOE or TPE for each element. For arrangements where VSOE or TPE cannot be established, the Company uses BESP for the allocation of arrangement consideration. The objective of BESP is to determine the price at which the Company would typically transact a standalone sale of the product or service. BESP is determined by considering a number of factors including the Company's pricing policies, internal costs and gross margin objectives, current market conditions, information gathered from experience in customer negotiations and the competitive landscape.

The Company enters into arrangements containing multiple elements which may include a combination of the sale of molds, tooling, engineering and validation services and production units. The Company has determined that sale of certain molds, tooling, engineering and validation services, and the production units, represent one unit of accounting, based on an assessment of the respective standalone value, as defined in ASC 605-25, “Revenue Recognition: Multiple-Element Arrangements.”

The Company evaluates the merits and individual uniqueness of each transaction, the related product(s), and the customer, to determine if the arrangement qualifies for revenue recognition as multiple element arrangements. The Company determined that the estimated product life-cycle, and historical knowledge of the customer will determine the appropriate life over which the deferred revenue will be amortized into revenue, which generally takes place within two to five years of the initiation of the arrangement. Revenue for the production units is recognized upon shipment.

The Company cannot adequately predict short-term or long-term future production units in a consistent and meaningful manner given the prototyping and sampling nature of these molds and associated products. Many of these products require validation of a new design or acceptable end product and their viability in their respective competitive marketplaces. Therefore, the future production possibilities are unpredictable and sometimes volatile making the Company unable to account for the transactions under the Units of Production method. Therefore, management has determined that the most appropriate method of amortizing the amounts into revenue is the straight-line method. The life over which the deferred revenue will be amortized into revenue will be determined based upon the terms of the arrangement, estimated product life-cycle, historical knowledge of the customer and any other relevant information. Management estimates that the amortization of the arrangements will generally take place over a two to five year period.

Furthermore, the Company will use these factors in determining when it may be appropriate to accelerate remaining deferred revenue into income for products for customers who may have excessive time lags between the making of the mold and the production of units from the mold. Product life-cycles, customer supply chains, customer financial performance and other items may be indicators to management that realization of future production orders for the product may be more likely than not or improbable. At such point, management may determine, in its estimates, that it is appropriate to recognize the remaining revenue.

In connection with the preparation of the consolidated financial statements for the year ended December 31, 2012, the Company reviewed the accounting treatment of revenue recognition for certain molds, tooling and validation services (collectively “Tooling”) and their relation to molding or machining of production units for sale to the customer. As a result of such review, management determined that the Company had been incorrectly recognizing revenue for certain

Tooling transactions by not deferring the related revenue in accordance with guidance set forth in ASC 605-25, “Revenue Recognition: Multiple-Element Arrangements.”

In 2012, the Company determined that the errors were immaterial to the overall presentation of prior year financial statements and therefore revised the prior years as more fully described in the Company's Annual Report on Form 10-K for the year ended December 31, 2012. The revised March 31, 2012 financial statements are presented in this Form 10-Q as more fully described in Note 11.

The Company also recognizes revenue in accordance with ASC 985-605 "Software - Revenue Recognition" for software licenses it sells. Revenue is recognized when licenses are sold as the revenue cycle is completed with no warranty, returns or technical support to customers. Total revenue from software sales was immaterial in relation to consolidated revenues.

Fair value of financial instruments

The carrying amount reported in the balance sheets for cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities approximate their fair value due to the immediate or short-term nature of such instruments. The carrying amount of the Company's long-term and respective short-term portion of Equipment notes were $209,389 and $1,093,526, at March 31, 2013 as compared to 991,213 and $267,043 at December 31, 2012. These amounts approximate the fair value of these instruments as these notes were paid in full on April 4, 2013.

In addition to the Equipment notes, the Company had a line of credit with an outstanding balance of $800,000 at both March 31, 2013 and December 31, 2012 which approximates the fair value of this instrument due to the variable interest rates.

The Equipment notes and the line of credit were both paid off and closed on April 4, 2013 as part of the new bank facility as more fully described in Note 5.

Concentration of credit risk

Financial instruments which potentially expose the Company to concentrations of credit risk, as defined by Accounting Standards Codification ("ASC") 310 "Receivables", consist primarily of trade accounts receivable and cash. Accounts receivable are customer obligations due under normal trade terms. A large portion of the Company's products are sold to large diversified medical and defense product manufacturers. The Company does not generally require collateral for its sales; however, the Company believes that its terms of sale provide adequate protection against significant credit risk. Currently, the Company generally does not receive purchase volume commitments extending beyond several months. Large corporations can shift focus away from a need for the Company's products and services with little or no warning. The loss of any one or more of these customers may have an immediate significant adverse effect on our financial results.

It is the Company's policy to place its cash in high quality financial institutions. The Company does not believe significant credit risk exists above federally insured limits with respect to these institutions.

Cash and cash equivalents

Cash and cash equivalents consist of cash on hand and on deposit in high quality financial institutions with maturities of three months or less at the time of purchase.

Allowance for Doubtful Accounts

Management regularly reviews accounts receivable to determine if any receivables will potentially be uncollectible. The Company includes any accounts receivable balances that are determined to be uncollectible, along with a general reserve, in the Company's overall allowance for doubtful accounts. After all attempts to collect a receivable have failed, the receivable is written off against the allowance. Based on the information available to the Company, management believes the allowance for doubtful accounts of $117,098 as of March 31, 2013 and December 31, 2012 is adequate.

Inventories

The Company values its inventory at the lower of average cost (FIFO) or net realizable value. The Company reviews its inventory for quantities in excess of production requirements, obsolescence and for compliance with internal quality specifications. Any adjustments to inventory would be equal to the difference between the cost of inventory and the estimated net market value based upon assumptions about future demand, market conditions and expected cost to distribute those products to market. The Company records adjustments to account for potential scrap during normal manufacturing operations or potential obsolescence for slow moving inventory.

Prepaid Tooling

Costs related to the pre-production design and development for certain molds, tooling and validation services (collectively "Tooling") are classified as other current and other non-current assets as applicable. Prepaid Tooling costs include such costs associated with the production of tools sold to customers, for which the Company is recording corresponding deferred revenue. As deferred revenue is amortized into revenue, the associated prepaid tooling costs are expensed to cost of sales.

Plant, property and equipment

Property, plant and equipment are recorded at cost and include expenditures which substantially extend their useful lives. Depreciation on property, plant and equipment is calculated using the straight-line method over the estimated useful lives of the assets. Expenditures for maintenance and repairs are charged to earnings as incurred. When equipment is retired or sold, the resulting gain or loss is reflected in earnings.

Long-Lived and Intangible Assets
In accordance with ASC 360, "Long-Lived Assets," the Company assesses the impairment of long-lived assets and intangible assets with finite lives whenever events or changes in circumstances indicate that the carrying value may not be fully recoverable. There were no such triggering events for the three months ended March 31, 2013 or 2012.
Intangible assets consist of the following:

	March 31, 2013				December 31, 2012		
	Weighted average remaining life (years)	Gross	Accumulated Amortization	Net	Gross	Accumulated Amortization	Net
Patents and Trademarks	13	$445,063	$(421,892)	$23,171	$445,063	$(420,675)	$24,388
Patents and Trademarks*	—	143,531	—	143,531	110,703	—	110,703
Trade names	9	33,250	(12,833)	20,417	33,250	(12,250)	21,000
Total Intangible assets:		$621,844	$(434,725)	$187,119	$589,016	$(432,925)	$156,091

* Patents and Trademarks not yet in service.

Income taxes
The Company accounts for income taxes in accordance with ASC 740 “Income Taxes,” which requires recognition of deferred tax liabilities and assets for the expected future tax consequences of events that have been included in the financial statements or tax returns. Under this method, deferred tax liabilities and assets are determined based on the difference between the financial statement and tax bases of assets and liabilities using tax rates in effect for the year in which the differences are expected to reverse. For the periods ended March 31, 2013 and December 31, 2012, no valuation allowance has been recorded against deferred tax assets from continuing operations.
The Company recorded a valuation allowance against certain foreign and state deferred tax assets associated with discontinued operations. For the year ended December 31, 2012, a valuation allowance of $470,900 was maintained against these assets for which the realization of tax benefit is not more likely than not. Management determined that no change was necessary in the valuation allowance for the period ended March 31, 2013.

Share-based compensation
The Company accounts for share-based compensation under the provisions of ASC 718 “Stock Compensation,” which establishes accounting for equity instruments exchanged for employee services. Under ASC 718, share-based compensation cost is measured at the grant date, based on the fair value of the award, and is recognized as an expense over the employee’s requisite service period (generally the vesting period of the equity grant).

Comprehensive income
The Company follows the provisions of ASC 220 “Comprehensive Income,” which establishes standards for reporting and display of comprehensive income, its components, and accumulated balances. Comprehensive income is defined to include all changes in equity, except those resulting from investments by owners and distributions to owners. There were no changes in comprehensive income in the three months ended March 31, 2013. The Company has accumulated comprehensive income of $42,502 from changes in currency valuations with our discontinued Canadian operations as of March 31, 2013 and December 31, 2012.

Preferred stock
The Company has 2,000,000 shares of $1 par value preferred stock authorized. No shares have been issued.

(Loss) earnings per share data
The Company follows the provisions of ASC 260 “Earnings Per Share,” which requires the Company to present its basic earnings per share and diluted earnings per share, and certain other earnings per share disclosures for each year presented. Basic earnings per share is computed by dividing income available to common shareholders by the weighted average number of common shares outstanding. The computation of diluted earnings per share is similar to the computation of basic earnings per share except that the denominator is increased to include the average number of additional common shares that would have been outstanding if the dilutive potential common shares had been issued. In addition, the numerator is adjusted for any changes in income that would result from the assumed conversions of those potential shares. As of March 31, 2013 and December 31, 2012 there were 263,000and 285,000

options outstanding, respectively, that were anti-dilutive and were not included in the calculation of earnings or loss per share.

Basic and diluted EPS computations are as follows:

Three months ended March 31,	2013	Revised 2012
Net loss available to common shareholders	$ (5,671)	$ (435,919)
Weighted average common shares outstanding	2,704,239	2,790,514
(Loss) income per share - basic		
Continuing Operations	0.00	0.12
Discontinued Operations	0.00	(0.28)
Loss per share - basic	$ 0.00	$ (0.16)
Net loss available to common shareholders	$ (5,671)	$ (435,919)
Weighted average common shares outstanding, basic	2,704,239	2,790,514
Assumed conversion of net common shares issuable under stock option plans	—	—
Weighted average common and common equivalent shares outstanding, diluted	2,704,239	2,790,514
(Loss) income per share - diluted		
Continuing Operations	0.00	0.12
Discontinued Operations	0.00	(0.28)
Loss per share - diluted	$ 0.00	$ (0.16)

Segments

The Company follows the provisions of ASC 280 “Segment Reporting,” which requires reporting of selected information about operating segments in interim and annual financial statements issued to the public. It also establishes standards for disclosures regarding products and services, geographic areas, and major customers. ASC 280 defines operating segments as components of an enterprise that engage in business activities that may earn revenues and incur expenses, which have separate financial information available, and are evaluated regularly by the Chief Operating Decision Maker ("CODM") in deciding how to allocate resources and in assessing performance.

In 2012, the Company determined that the Company's results will be reported as one segment due to the discontinued operations of its WirelessDx segment and since the results of its previously reported ART segment were not quantitatively material and were not regularly reviewed by the CODM. The results of the three months ended March 31, 2012 have been reclassified accordingly.

Research and development

Research and development expenses include costs directly attributable to the conduct of research and development programs primarily related to the development of our software products and improving the efficiency and capabilities of our manufacturing processes. Such costs include salaries, payroll taxes, employee benefit costs, materials, supplies, depreciation on research equipment, and services provided by outside contractors. All costs associated with research and development programs are expensed as incurred.

Recent accounting pronouncements

In January 2013, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2013-01 Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities. The main objective of this update is to address implementation issues about the scope of ASU 2011-11 Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities as well as to clarify the scope of the offsetting disclosures and address any unintended consequences of ASU 2011-11. This update helps clarify the scope of disclosures as they apply to derivatives accounted for in accordance with Topic 815 Derivatives and Hedging. An entity is required to apply the amendments for fiscal years beginning on or after January 1, 2013 and provide the required disclosures retrospectively for all comparative periods presented. At present the Company does not have any derivatives as outlined in Topic 815, including bifurcated embedded derivatives, repurchase agreements and reverse repurchase agreements, or securities borrowings or securities lending transactions. As such, the Company does not expect this update to have a material impact on the Company's results of operations or financial position.

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Reclassifications

Certain reclassifications have been made to prior period amounts to conform to the current period presentation, primarily related to discontinued operations and deferred revenue. In the third quarter of 2012, the Company discontinued the operations of the Company's WirelessDx subsidiaries and has therefore reclassified the March 31, 2012 results of the WirelessDx subsidiaries as discontinued operations. In 2012, the Company revised prior period balances to correct errors in the revenue recognition of certain Tooling transactions (Note 11).

3. Inventories

Inventories consist of the following:

	March 31, 2013	December 31, 2012
Raw materials	$1,037,061	$521,908
Work-in-process	334,284	248,159
Finished goods	1,388,308	1,645,037
Total	$2,759,653	$2,415,104

The value of silver in inventory at March 31, 2013 and December 31, 2012 as a part of finished goods as plated sensors, work in process, or raw materials was $551,399 and $541,804, respectively. Inventories are stated at their net realizable value, net of a reserve for slow moving and obsolete inventory of $339,984 and $317,484 at March 31, 2013 and December 31, 2012, respectively.

4. Plant, property and equipment, net

Property, plant and equipment consist of the following:

	Asset lives (in years)	March 31, 2013	December 31, 2012
Machinery and equipment	3 to 15	$12,578,110	$12,298,011
Building and improvements	20	4,293,725	4,293,725
Vehicles	3 to 5	94,227	94,227
Furniture, fixtures, computers and software	3 to 5	1,250,471	1,246,807
Land		202,492	202,492
Construction in progress		125,046	103,269
Total property, plant and equipment		18,544,071	18,238,531
Less: accumulated depreciation		(11,408,053)	(11,080,019)
Property, plant and equipment, net		$7,136,018	$7,158,512

For the three months ended March 31, 2013 and 2012 the Company recorded $336,743 and $347,797 of depreciation expense, respectively.

5. Debt

As of March 31, 2013 and December 31, 2012, the Company had the following outstanding debt:

	March 31, 2013	December 31, 2012
Demand line of credit	$800,000	$800,000
Debt:		
Equipment notes	$1,302,915	$1,258,256
Less current portion	1,093,526	267,043
Total long-term debt	$209,389	$991,213

At March 31, 2013, the Company had a demand line of credit that provided for borrowings up to 80% of eligible accounts receivable and eligible finished goods inventory up to $700,000 at a rate of 2% over LIBOR. The interest rate at March 31, 2013 and December 31, 2012 was4.20% and 2.21%, respectively. This facility has no borrowing base charge. There were no additional borrowings on this line during the three months ended March 31, 2013. The outstanding principal balance at March 31, 2013 was $800,000. The demand line of credit had a maturity date of April 30, 2013.

The borrowing agreement contained covenants that applied upon drawing on the line. The covenants related to various matters including notice prior to executing further borrowings and security interests, merger or consolidation, acquisitions, guarantees, sales of assets other than in the normal course of business, leasing, changes in ownership and payment of dividends. This line of credit was paid off and closed on April 4, 2013 as it was refinanced by a new bank facility as described more fully below.

Also, secured by this credit line, the Company had a $1,000,000 letter of credit for a performance guarantee associated with the discontinued operations. This liability is being carried on the balance sheet of continuing operations, as the letter of credit is guaranteed by ART.

During the three months ended March 31, 2013, the Company entered into two new Equipment notes totaling $272,500 with a financing company, to acquire production equipment. As of March 31, 2013, the outstanding balance of these Equipment notes was $259,321. The term of these Equipment notes is five years.

At March 31, 2012, the Company had a master lease agreement with its bank that allowed for money to be drawn on standard terms for the purchase of equipment. During the three months ended March 31, 2012, the Company entered into a new Equipment note for $523,269. This note was structured in such a way that the Company received a cash payout for amounts already paid to vendors of $262,960, with the remaining $260,309 paid by the bank directly to the vendors making total principal amount of the Equipment note entered into $523,269. The cash payout is shown as proceeds from Equipment note on the statement of cash flows for the three months ended March 31, 2012. The remaining amount of $260,309 was a non-cash event and is disclosed in the supplemental cash flow schedule.

The outstanding balances of all Equipment notes under this master lease agreement at March 31, 2013 and December 31, 2012 were $1,302,915 and $1,258,256, respectively. The term of these Equipment notes is five years. The Equipment notes under this master lease agreement were paid off on April 4, 2013, as part of a new bank facility as described more fully below.

On, March 29, 2013, the Company entered into a multi-year credit facility with a Massachusetts based bank to replace the existing demand line of credit. The new credit facility includes a revolving line of credit of up to $4.0 million, a commercial term loan of $1.5 million and an equipment line of credit of $1.0 million.