CUTERA INC
Form 10-Q
November 05, 2012

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 September 30, 2012

OR

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

For the transition period _____ to_____.

Commission file number: 000-50644

Cutera, Inc.
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	77-0492262 (I.R.S. employer identification no.)

3240 Bayshore Blvd., Brisbane, California 94005
(Address of principal executive offices)

(415) 657-5500
(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 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 x	Non-accelerated filer ¨	Smaller reporting company ¨

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

The number of shares of Registrant’s common stock issued and outstanding as of October 26, 2012 was 14,127,344.

CUTERA, INC.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

CUTERA, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands)

	September 30, 2012 (unaudited)	December 31, 2011 (audited)
Assets		
Current assets:		
Cash and cash equivalents	$ 24,334	$ 14,020
Marketable investments	55,795	74,666
Accounts receivable, net	7,845	5,193
Inventories	12,477	10,729
Deferred tax asset	49	55
Other current assets and prepaid expenses	1,443	1,432
Total current assets	101,943	106,095
Property and equipment, net	885	853
Long-term investments	1,050	3,027
Deferred tax asset, net of current portion	470	446
Intangibles, net	2,876	446
Goodwill	1,339	—
Other long-term assets	517	486
Total assets	$ 109,080	$ 111,353
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$ 2,297	$ 2,573
Accrued liabilities	9,486	9,262
Deferred revenue	6,299	5,185
Total current liabilities	18,082	17,020
Deferred rent	1,347	1,448
Deferred revenue, net of current portion	1,411	840
Income tax liability	471	478
Total liabilities	21,311	19,786
Commitments and Contingencies (Note 12)		
Stockholders’ equity:		
Convertible preferred stock, $0.001 par value; authorized: 5,000,000 shares; none issued and outstanding	—	—
	14	14

Common stock, $0.001 par value; authorized: 50,000,000 shares; issued and outstanding: 14,127,344 and 13,948,395 shares at September 30, 2012 and December 31, 2011, respectively				
Additional paid-in capital		98,865		95,719
Accumulated deficit		(10,950)		(3,325)
Accumulated other comprehensive loss		(160)		(841)
Total stockholders' equity		87,769		91,567
Total liabilities and stockholders' equity	$	109,080	$	111,353

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

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CUTERA, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share data)

(unaudited)

	Three Months Ended September 30, 2012	Three Months Ended September 30, 2011	Nine Months Ended September 30, 2012	Nine Months Ended September 30, 2011
Net revenue:				
Products	$ 15,128	$ 12,005	$ 42,138	$ 31,599
Service	4,298	3,227	12,606	10,149
Total net revenue	19,426	15,232	54,744	41,748
Cost of revenue:				
Products	6,618	4,580	19,237	12,078
Service	2,210	2,192	6,710	6,394
Total cost of revenue	8,828	6,772	25,947	18,472
Gross profit	10,598	8,460	28,797	23,276
Operating expenses:				
Sales and marketing	7,014	6,426	21,563	18,720
Research and development	2,217	2,352	6,305	6,828
General and administrative	2,475	2,310	8,824	7,226
Total operating expenses	11,706	11,088	36,692	32,774
Loss from operations	(1,108)	(2,628)	(7,895)	(9,498)
Interest and other income, net	152	91	392	474
Loss before income taxes	(956)	(2,537)	(7,503)	(9,024)
Provision (benefit) for income taxes	(64)	326	122	150
Net loss	$ (892)	$ (2,863)	$ (7,625)	$ (9,174)
Net loss per share:				
Basic and Diluted	$ (0.06)	$ (0.21)	$ (0.54)	$ (0.67)
Weighted-average number of shares used in per share calculations:				
Basic and Diluted	14,127	13,862	14,061	13,765

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

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CUTERA, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(in thousands)

(unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
Net loss	$ (892)	$ (2,863)	$ (7,625)	$ (9,174)
Other comprehensive income:				
Net change in unrealized gain on available-for-sale securities	267	35	804	725
Provision (benefit) for income taxes related to items of other comprehensive income	102	(262)	123	(194)
Other comprehensive income, net of tax	165	297	681	919
Comprehensive loss	$ (727)	$ (2,566)	$ (6,944)	$ (8,255)

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

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CUTERA, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(unaudited)

	Nine Months Ended September 30, 2012	Nine Months Ended September 30, 2011
Cash flows from operating activities:		
Net loss	$ (7,625)	$ (9,174)
Adjustments to reconcile net loss to net cash used in operating activities:		
Stock-based compensation	2,334	3,105
Tax benefit from stock-based compensation	—	21
Excess tax benefit related to stock-based compensation	—	(21)
Depreciation and amortization	1,186	483
Other	(113)	235
Changes in assets and liabilities:		
Accounts receivable	(2,698)	106
Inventories	(196)	(3,211)
Other current assets and prepaid expenses	717	1,951
Other long-term assets	(31)	(493)
Accounts payable	(276)	855
Accrued liabilities	(163)	1,086
Deferred rent	(24)	(10)
Deferred revenue	905	(698)
Income tax liability	(7)	12
Net cash used in operating activities	(5,991)	(5,753)
Cash flows from investing activities:		
Acquisition of property and equipment	(358)	(421)
Disposal of property and equipment	—	36
Business acquisition	(5,091)	—
Proceeds from sales of marketable and long-term investments	26,361	17,597
Proceeds from maturities of marketable investments	34,445	35,085
Purchase of marketable investments	(39,864)	(46,255)
Net cash provided by investing activities	15,493	6,042
Cash flows from financing activities:		
Proceeds from exercise of stock options and employee stock purchase plan	812	1,045
Excess tax benefit related to stock-based compensation	—	21
Net cash provided by financing activities	812	1,066
Net increase in cash and cash equivalents	10,314	1,355
Cash and cash equivalents at beginning of period	14,020	12,519
Cash and cash equivalents at end of period	$ 24,334	$ 13,874

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

CUTERA, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Summary of Significant Accounting Policies

Description of Operations and Principles of Consolidation.
Cutera, Inc. (Cutera or the Company) is a global provider of laser and light-based aesthetic systems for practitioners worldwide. The Company designs, develops, manufactures, and markets the CoolGlide, Xeo, Solera, GenesisPlus, Excel V and truSculpt product platforms for use by physicians and other qualified practitioners to allow its customers to offer safe and effective aesthetic treatments to their customers. The Xeo and Solera platforms offer multiple hand pieces and applications, which allow customers to upgrade their systems (Upgrade revenue). In addition to systems and Upgrade revenue, the Company generates revenue from the sale of post warranty service contracts, providing services for products that are out of warranty, and Titan hand piece refills. In Japan the Company also distributes third party manufactured dermal fillers, cosmeceuticals and a Q-switched laser system called myQ.

In February 2012, the Company acquired the global aesthetic business unit of IRIDEX Corporation (or Iridex), which included various laser systems (such as the VariLite and Gemini) and an installed base of customers, whose products are being serviced by the Company.

Headquartered in Brisbane, California, the Company has wholly-owned subsidiaries in Australia, Canada, and France and Japan that market, sell and service its products outside of the United States. Effective March 31, 2012, the Company decided to discontinue its direct operations in Spain and the United Kingdom and instead plans on seeking a distributor to market its products in these countries. The Condensed Consolidated Financial Statements include the accounts of the Company and its subsidiaries and all inter-company transactions and balances have been eliminated.

Unaudited Interim Financial Information
The financial information filed is unaudited. The Condensed Consolidated Financial Statements included in this report reflect all adjustments (consisting only of normal recurring adjustments) that the Company considers necessary for the fair statement of the results of operations for the interim periods covered and of the financial condition of the Company at the date of the interim balance sheet. The December 31, 2011 Condensed Consolidated Balance Sheet was derived from audited financial statements, but does not include all disclosures required by generally accepted accounting principles in the United States of America (GAAP). The results for interim periods are not necessarily indicative of the results for the entire year or any other interim period. The Condensed Consolidated Financial Statements should be read in conjunction with the Company’s financial statements and the notes thereto included in the Company’s annual report on Form 10-K for the year ended December 31, 2011 filed with the Securities and Exchange Commission, or SEC, on March 15, 2012.

Use of Estimates
The preparation of interim Condensed Consolidated Financial Statements in conformity with GAAP requires the Company’s management to make estimates and assumptions that affect the amounts reported and disclosed in the Condensed Consolidated Financial Statements and the accompanying notes. Actual results could differ materially from those estimates. On an ongoing basis, the Company evaluates these estimates, including those related to warranty obligation, sales commission, accounts receivable and sales allowances, provision for excess and obsolete inventories, fair values of marketable and long-term investments, fair values of acquired intangible assets, useful lives of intangible assets and property and equipment, recoverability of deferred tax assets, and effective income tax rates, among others. Management bases these estimates on historical experience and on various other assumptions that are believed to be reasonable, the results of which form the basis for making judgments about the carrying values of assets and liabilities.

Note 2. Cash and Cash Equivalents, Marketable Securities and Long-Term Investments

The Company considers all highly liquid investments, with an original maturity of three months or less at the time of purchase, to be cash equivalents. Investments in debt securities are accounted for as “available-for-sale” securities, carried at fair value with unrealized gains and losses reported in other comprehensive loss, held for use in current operations and classified in current assets as “Marketable investments” and in long term assets as “Long-term investments.”

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The following tables summarize unrealized gains and losses related to our marketable investments and long-term investments, both designated as available-for-sale (in thousands):

September 30, 2012	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Market Value
Cash and cash equivalents:				
Cash	$ 1,853	$ —	$ —	$ 1,853
Money market funds	14,577	—	—	14,577
Commercial paper	7,904	—	—	7,904
Total cash and cash equivalents	24,334	—	—	24,334
Marketable securities:				
U.S. government agencies	23,884	51	(1)	23,934
Municipal securities	6,046	32	(1)	6,077
Commercial paper	7,507	2	—	7,509
Corporate debt securities	18,215	61	(1)	18,275
Total marketable investments	55,652	146	(3)	55,795
Long-term investment in auction rate securities	1,200	—	(150)	1,050
Total cash, cash equivalents, marketable investments and long-term investments	$ 81,186	$ 146	$ (153)	$ 81,179

December 31, 2011	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Market Value
Cash and cash equivalents:				
Cash	$ 2,153	$ —	$ —	$ 2,153
Money market funds	7,318	—	—	7,318
Commercial paper	4,549	—	—	4,549
Total cash and cash equivalents	14,020	—	—	14,020
Marketable securities:				
U.S. government notes	3,655	10	—	3,665
U.S. government agencies	41,535	44	(14)	41,565
Municipal securities	6,091	44	(1)	6,134
Commercial paper	4,747	1	(1)	4,747
Corporate debt securities	18,574	15	(34)	18,555
Total marketable investments	74,602	114	(50)	74,666
Long-term investment in auction rate securities	3,900	—	(873)	3,027
Total cash, cash equivalents, marketable investments and long-term investments	$ 92,522	$ 114	$ (923)	$ 91,713

As of September 30, 2012 and December 31, 2011, the total gross unrealized losses were $153,000 and $923,000 respectively and were primarily related to long-term investments in auction rate securities (ARS), which were in an unrealized loss position for 12 months or greater. No other securities were in unrealized loss positions for more than 12 months. The unrealized losses in the ARS securities are not attributed to changes in credit risk and the Company does not intend to sell the investments and it is not more likely than not that the Company will be required to sell the investments before recovery of their amortized cost bases, which may be maturity.

Since February 2008, uncertainties in the credit markets affected the majority of ARS investments and auctions for the Company’s investments in these securities have failed to settle on their respective settlement dates. However, since 2009 $12.2 million of ARS were redeemed at full par value. The maturity date for the one remaining ARS investment in the Company’s portfolio is 2041.

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The following table summarizes the estimated fair value of our securities available-for-sale and classified as cash and cash equivalents, marketable investments and long-term investments classified by the contractual maturity date of the security as of September 30, 2012 (in thousands):

	Amount
Due in less than one year	$ 35,073
Due in 1 to 5 years	28,626
Due in 5 to 10 years	—
Due in greater than 10 years	1,050
	$ 64,749

Note 3. Fair Value of Financial Instruments

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value hierarchy distinguishes between (1) market participant assumptions developed based on market data obtained from independent sources (observable inputs) and (2) an entity's own assumptions about market participant assumptions developed based on the best information available in the circumstances (unobservable inputs). The fair value hierarchy consists of three broad levels, which 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: Quoted prices (unadjusted) in active markets that are accessible at the measurement date for assets or liabilities.

Level 2: Directly or indirectly observable inputs as of the reporting date through correlation with market data, including quoted prices for similar assets and liabilities in active markets and quoted prices in markets that are not active. Level 2 also includes assets and liabilities that are valued using models or other pricing methodologies that do not require significant judgment since the input assumptions used in the models, such as interest rates and volatility factors, are corroborated by readily observable data from actively quoted markets for substantially the full term of the financial instrument.

Level 3: Unobservable inputs that are supported by little or no market activity 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.

In determining fair value, the Company utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible as well as considers counterparty credit risk in its assessment of fair value.

As of September 30, 2012, financial assets measured and recognized at fair value on a recurring basis and classified under the appropriate level of the fair value hierarchy as described above was as follows (in thousands):

September 30, 2012	Level 1	Level 2	Level 3	Total
Cash equivalents:				
Money market funds	$ 14,577	—	—	$ 14,577
Commercial paper	—	7,904	—	7,904
Short-term marketable investments:				
U.S. government agencies	—	23,934	—	23,934
Municipal securities	—	6,077	—	6,077
Commercial paper	—	7,509	—	7,509
Corporate debt securities	—	18,275	—	18,275

Long-term investments:				
Available-for-sale auction rate securities	—	—	1,050	1,050
Total assets at fair value	$ 14,577	$ 63,699	$ 1,050	$ 79,326

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As of December 31, 2011, financial assets measured and recognized at fair value on a recurring basis and classified under the appropriate level of the fair value hierarchy as described above was as follows (in thousands):

December 31, 2011	Level 1	Level 2	Level 3	Total
Cash equivalents:				
Money market funds	$ 7,318	—	—	$ 7,318
Commercial paper	—	4,549	—	4,549
Short-term marketable investments:				
U.S. government notes	—	3,665	—	3,665
U.S. government agencies	—	41,565	—	41,565
Municipal securities	—	6,134	—	6,134
Commercial paper	—	4,747	—	