

ICAD INC  
Form 10-Q  
November 14, 2017  
Table of Contents

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**WASHINGTON, D.C. 20549**

**FORM 10-Q**

(Mark One)

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

**For the quarterly period ended September 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 001-09341**

**iCAD, Inc.**

**(Exact name of registrant as specified in its charter)**

**Delaware**  
**(State or other jurisdiction of**  
**incorporation or organization)**

**02-0377419**  
**(I.R.S. Employer**  
**Identification No.)**

**98 Spit Brook Road, Suite 100, Nashua, NH**  
**(Address of principal executive offices)**  
**(603) 882-5200**

**03062**  
**(Zip Code)**

**(Registrant's telephone number, including area code)**

**Not Applicable**

**(Former name, former address and former fiscal year, if changed since last report)**

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 requirement for the past 90 days. YES 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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES NO .

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, an emerging growth company or a smaller reporting 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.

Large Accelerated filer

Accelerated filer

Non-accelerated filer (do not check if a smaller reporting company)

Smaller reporting company

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 .

Edgar Filing: ICAD INC - Form 10-Q

As of the close of business on November 13, 2017 there were 16,511,655 shares outstanding of the registrant's Common Stock, \$.01 par value.

**Table of Contents**

iCAD, Inc.

INDEX

	Page
<b>PART I FINANCIAL INFORMATION</b>	
Item 1 Financial Statements (unaudited)	
<u>Condensed Consolidated Balance Sheets as of September 30, 2017 and December 31, 2016</u>	3
<u>Condensed Consolidated Statements of Operations for the three and nine months ended September 30, 2017 and September 30, 2016</u>	4
<u>Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2017 and September 30, 2016</u>	5
<u>Notes to Condensed Consolidated Financial Statements</u>	6-28
Item 2 <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	29-41
Item 3 <u>Quantitative and Qualitative Disclosures about Market Risk</u>	42
Item 4 <u>Controls and Procedures</u>	42
<b>PART II OTHER INFORMATION</b>	
Item 1 <u>Legal Proceedings</u>	43
Item 1A <u>Risk Factors</u>	43
Item 2 <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	43
Item 6 <u>Exhibits</u>	43
<u>Signatures</u>	45

Table of Contents

**iCAD, INC. AND SUBSIDIARIES**  
**Condensed Consolidated Balance Sheets**

(Unaudited)

(In thousands except for share data)

	September 30, 2017	December 31, 2016
<u>Assets</u>		
Current assets:		
Cash and cash equivalents	\$ 11,261	\$ 8,585
Trade accounts receivable, net of allowance for doubtful accounts of \$209 in 2017 and \$172 in 2016	7,189	5,189
Inventory, net	3,340	3,727
Prepaid expenses and other current assets	949	1,128
Assets held for sale		1,304
Total current assets	22,739	19,933
Property and equipment, net of accumulated depreciation of \$7,245 in 2017 and \$6,538 in 2016	972	1,385
Other assets	53	53
Intangible assets, net of accumulated amortization of \$7,333 in 2017 and \$7,518 in 2016	2,055	3,183
Goodwill	10,128	14,097
Total assets	\$ 35,947	\$ 38,651
<u>Liabilities and Stockholders' Equity</u>		
Current liabilities:		
Accounts payable	\$ 1,346	\$ 1,577
Accrued and other expenses	4,935	4,988
Lease payable - current portion	12	86
Notes payable - current portion	317	
Liabilities held for sale		832
Deferred revenue	5,021	5,372
Total current liabilities	11,631	12,855
Other long-term liabilities	140	83
Lease payable, long-term portion	30	
Notes payable, long-term portion	5,612	
Deferred revenue, long-term portion	525	668
Deferred tax	12	7

Total liabilities	17,950	13,613
<b>Commitments and Contingencies (Note 6, 7 and 9)</b>		
Stockholders' equity:		
Preferred stock, \$ .01 par value: authorized 1,000,000 shares; none issued.		
Common stock, \$ .01 par value: authorized 30,000,000 shares; issued 16,627,705 in 2017 and 16,260,663 in 2016; outstanding 16,441,874 in 2017 and 16,074,832 in 2016		
Additional paid-in capital	167	163
Accumulated deficit	216,875	213,899
Treasury stock at cost, 185,831 shares in 2017 and 2016	(197,630)	(187,609)
	(1,415)	(1,415)
Total stockholders' equity	17,997	25,038
Total liabilities and stockholders' equity	\$ 35,947	\$ 38,651

*See accompanying notes to condensed consolidated financial statements.*

**Table of Contents****iCAD, INC. AND SUBSIDIARIES****Condensed Consolidated Statements of Operations**

(Unaudited)

(In thousands except for per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
<b>Revenue:</b>				
Products	\$ 3,426	\$ 2,014	\$ 9,225	\$ 7,460
Service and supplies	3,574	3,989	10,975	11,950
<b>Total revenue</b>	<b>7,000</b>	<b>6,003</b>	<b>20,200</b>	<b>19,410</b>
<b>Cost of revenue:</b>				
Products	636	236	1,349	611
Service and supplies	1,458	1,370	4,169	3,911
Amortization and depreciation	263	296	847	899
<b>Total cost of revenue</b>	<b>2,357</b>	<b>1,902</b>	<b>6,365</b>	<b>5,421</b>
<b>Gross profit</b>	<b>4,643</b>	<b>4,101</b>	<b>13,835</b>	<b>13,989</b>
<b>Operating expenses:</b>				
Engineering and product development	2,254	2,360	7,060	6,835
Marketing and sales	2,580	2,322	8,172	7,379
General and administrative	1,944	1,783	6,067	5,586
Amortization and depreciation	107	288	345	867
Gain on sale of MRI assets			(2,508)	
Goodwill and long-lived asset impairment	4,700		4,700	
<b>Total operating expenses</b>	<b>11,585</b>	<b>6,753</b>	<b>23,836</b>	<b>20,667</b>
<b>Loss from operations</b>	<b>(6,942)</b>	<b>(2,652)</b>	<b>(10,001)</b>	<b>(6,678)</b>
Interest expense	(36)	(15)	(51)	(59)
Other income	3	2	3	9
<b>Other expense, net</b>	<b>(33)</b>	<b>(13)</b>	<b>(48)</b>	<b>(50)</b>
<b>Loss before income tax expense</b>	<b>(6,975)</b>	<b>(2,665)</b>	<b>(10,049)</b>	<b>(6,728)</b>
Tax benefit (expense)	42	(10)	28	(55)
<b>Net loss and comprehensive loss</b>	<b>\$ (6,933)</b>	<b>\$ (2,675)</b>	<b>\$ (10,021)</b>	<b>\$ (6,783)</b>
<b>Net loss per share:</b>				
Basic	\$ (0.42)	\$ (0.17)	\$ (0.62)	\$ (0.43)

Edgar Filing: ICAD INC - Form 10-Q

Diluted	\$	(0.42)	\$	(0.17)	\$	(0.62)	\$	(0.43)
Weighted average number of shares used in computing loss per share:								
Basic		16,424		15,957		16,291		15,896
Diluted		16,424		15,957		16,291		15,896

*See accompanying notes to consolidated financial statements.*



**Table of Contents****iCAD, INC. AND SUBSIDIARIES****Condensed Consolidated Statements of Cash Flows**

(unaudited)

	<b>For the nine months ended September 30,</b>	
	<b>2017</b>	<b>2016</b>
	(in thousands)	
<b>Cash flow from operating activities:</b>		
Net loss	\$ (10,021)	\$ (6,783)
<b>Adjustments to reconcile net loss to net cash used for by operating activities:</b>		
Amortization	394	753
Depreciation	798	1,013
Bad debt provision	44	133
Stock-based compensation expense	3,073	1,648
Amortization of debt discount and debt costs	(6)	(13)
Interest on settlement obligations	26	69
Deferred tax expense	6	
Gain from acquisition litigation settlement		(249)
Goodwill and long-lived asset impairment	4,700	
Loss on disposal of assets	26	9
Gain on sale of MRI assets	(2,158)	
<b>Changes in operating assets and liabilities (net of the effect of acquisitions):</b>		
Accounts receivable	(2,062)	2,706
Inventory	389	(82)
Prepaid and other current assets	179	(483)
Accounts payable	(231)	(281)
Accrued expenses	(23)	78
Deferred revenue	(699)	(2,380)
Total adjustments	4,456	2,921
<b>Net cash used for operating activities</b>	<b>(5,565)</b>	<b>(3,862)</b>
<b>Cash flow from investing activities:</b>		
Additions to patents, technology and other	(2)	(8)
Additions to property and equipment	(362)	(248)
Acquisition of VuComp M-Vu CAD		(6)
Sale of MRI assets	2,850	
<b>Net cash provided by (used for) investing activities</b>	<b>2,486</b>	<b>(262)</b>
<b>Cash flow from financing activities:</b>		
Stock option exercises	57	188

Edgar Filing: ICAD INC - Form 10-Q

Taxes paid related to restricted stock issuance	(151)	(65)
Debt issuance costs	(74)	
Principal payments of capital lease obligations	(77)	(796)
Proceeds from debt financing, net	6,000	
Net cash provided by (used for) financing activities	5,755	(673)
Increase (decrease) in cash and equivalents	2,676	(4,797)
Cash and equivalents, beginning of period	8,585	15,280
Cash and equivalents, end of period	\$ 11,261	\$ 10,483
Supplemental disclosure of cash flow information:		
Interest paid	\$ 14	\$ 63
Taxes paid	\$ 52	\$ 65
Escrow due from MRI asset sale	\$ 350	\$
Equipment purchased under capital lease	\$ 42	\$

*See accompanying notes to consolidated financial statements.*

---

**Table of Contents**

**iCAD, INC. AND SUBSIDIARIES**

**Notes to Condensed Consolidated Financial Statements**

**(Unaudited)**

**September 30, 2017**

**Note 1 - Basis of Presentation and Significant Accounting Policies**

The accompanying condensed consolidated financial statements of iCAD, Inc. and subsidiaries ( iCAD or the Company ) have been prepared in accordance with accounting principles generally accepted in the United States of America ( US GAAP ). In the opinion of management, these unaudited interim condensed consolidated financial statements reflect all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of the financial position of the Company at September 30, 2017, the results of operations of the Company for the three and nine month periods ended September 30, 2017 and 2016, and cash flows of the Company for the nine month periods ended September 30, 2017 and 2016. Although the Company believes that the disclosures in these financial statements are adequate to make the information presented not misleading, certain information normally included in the footnotes prepared in accordance with US GAAP has been omitted as permitted by the rules and regulations of the Securities and Exchange Commission ( SEC ). The accompanying financial statements should be read in conjunction with the audited financial statements and notes thereto included in the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2016 filed with the SEC on March 24, 2017. The results for the three and nine month periods ended September 30, 2017 are not necessarily indicative of the results that may be expected for the fiscal year ending December 31, 2017, or any future period.

*Segments*

The Company reports the results of two segments: Cancer Detection ( Detection ) and Cancer Therapy ( Therapy ). The Detection segment consists of our advanced image analysis and workflow products. The Therapy segment consists of our radiation therapy ( Axxent ) products, physics and management services, development fees, supplies, and fees for the AxxentHub software platform.

*Revenue Recognition*

The Company recognizes revenue primarily from the sale of products and from the sale of services and supplies. Revenue is recognized when delivery has occurred, persuasive evidence of an arrangement exists, fees are fixed or determinable and collectability of the related receivable is probable. For product revenue, delivery has occurred upon shipment provided title and risk of loss have passed to the customer. Services and supplies revenue are considered to be delivered as the services are performed or over the estimated life of the supply agreement.

The Company recognizes revenue from the sale of its digital, film-based CAD and cancer therapy products and services in accordance with Financial Accounting Standards Board ( FASB ) Accounting Standards Codification ( ASC ) Update No. 2009-13, Multiple-Deliverable Revenue Arrangements ( ASU 2009-13 ) and ASC Update No. 2009-14, Certain Arrangements That Contain Software Elements ( ASU 2009-14 ) and ASC 985-605, Software ( ASC 985-605). Revenue from the sale of certain CAD products is



---

**Table of Contents**

**iCAD, INC. AND SUBSIDIARIES**

**Notes to Condensed Consolidated Financial Statements**

**(Unaudited)**

**September 30, 2017**

recognized in accordance with ASC 840 Leases ( ASC 840 ). For multiple element arrangements, revenue is allocated to all deliverables based on their relative selling prices. In such circumstances, a hierarchy is used to determine the selling price to be used for allocating revenue to deliverables as follows: (i) vendor-specific objective evidence of fair value ( VSOE ), (ii) third-party evidence of selling price ( TPE ) and (iii) best estimate of the selling price ( BEBP ). VSOE generally exists only when the deliverable is sold separately and is the price actually charged for that deliverable. The process for determining BEBP for deliverables without VSOE or TPE considers multiple factors including relative selling prices; competitive prices in the marketplace, and management judgment; however, these may vary depending upon the unique facts and circumstances related to each deliverable.

The Company uses customer purchase orders that are subject to the Company's terms and conditions or, in the case of an Original Equipment Manufacturer ( OEM ) are governed by distribution agreements. In accordance with the Company's distribution agreements, the OEM does not have a right of return, and title and risk of loss passes to the OEM upon shipment. The Company generally ships Free On Board shipping point and uses shipping documents and third-party proof of delivery to verify delivery and transfer of title. In addition, the Company assesses whether collection is probable by considering a number of factors, including past transaction history with the customer and the creditworthiness of the customer, as obtained from third party credit references.

If the terms of the sale include customer acceptance provisions and compliance with those provisions cannot be demonstrated, all revenue is deferred and not recognized until such acceptance occurs. The Company considers all relevant facts and circumstances in determining when to recognize revenue, including contractual obligations to the customer, the customer's post-delivery acceptance provisions, if any, and the installation process.

The Company has determined that iCAD's digital and film based sales generally follow the guidance of FASB ASC Topic 605 Revenue Recognition ( ASC 605 ) as the software has been considered essential to the functionality of the product per the guidance of ASU 2009-14. Typically, the responsibility for the installation process lies with the OEM partner. On occasion, when iCAD is responsible for product installation, the installation element is considered a separate unit of accounting because the delivered product has stand-alone value to the customer. In these instances, the Company allocates revenue to the deliverables based on the framework established within ASU 2009-13. Therefore, the installation and training revenue is recognized as the services are performed according to the BEBP of the element. Revenue from the digital and film based equipment, when there is installation, is recognized based on the relative selling price allocation of the BEBP, when delivered.

Revenue from certain CAD products is recognized in accordance with ASC 985-605. Sales of these products include training, and the Company has established VSOE for this element. Product revenue is determined based on the residual value in the arrangement and is recognized when delivered. Revenue for training is deferred and recognized when the training has been completed.



**Table of Contents**

**iCAD, INC. AND SUBSIDIARIES**

**Notes to Condensed Consolidated Financial Statements**

**(Unaudited)**

**September 30, 2017**

The Company recognizes post contract customer support revenue together with the initial licensing fee for certain MRI products in accordance with ASC 985-605-25-71. In January 2017 the Company sold certain MRI assets to Invivo.

Sales of the Company's Therapy segment products typically include a controller, accessories, source agreements and services. The Company allocates revenue to the deliverables in the arrangement based on the BEP in accordance with ASU 2009-13. Product revenue is generally recognized when the product has been delivered and service and source revenue is typically recognized over the life of the service and source agreement. The Company includes the following in service and supplies revenue: the sale of physics and management services, the lease of electronic brachytherapy equipment, development fees, supplies and the right to use the Company's AxxentHub software. Physics and management services revenue and development fees are considered to be delivered as the services are performed or over the estimated life of the agreement. The Company typically bills items monthly over the life of the agreement except for development fees, which are generally billed in advance or over a 12 month period and the fee for treatment supplies which is generally billed in advance.

The Company defers revenue from the sale of certain service contracts and recognizes the related revenue on a straight-line basis in accordance with ASC Topic 605-20, Services. The Company provides for estimated warranty costs on original product warranties at the time of sale.

*Cost of Revenue*

Cost of revenue consists of the costs of products purchased for resale, costs relating to service including personnel costs for physicists, management services and radiation therapists, costs of service contracts to maintain equipment after the warranty period, product installation, training, customer support, certain warranty repair costs, inbound freight and duty, cost of supplies, manufacturing, warehousing, material movement, inspection, scrap, rework, amortization, depreciation and in-house product warranty repairs. Included in cost of revenue for the nine months ended September 30, 2016 is a credit of \$467,000 related to a refund of the Medical Device Excise Tax (MDET). The MDET refund of \$467,000 is related to refunds of the MDET for the periods from April 2013 to December 2015. The MDET refunds were not material to any prior period; accordingly, prior periods were not restated.

Table of Contents**iCAD, INC. AND SUBSIDIARIES****Notes to Condensed Consolidated Financial Statements****(Unaudited)****September 30, 2017****Note 2 - Loss per Common Share**

The Company's basic net loss per share is computed by dividing net loss by the weighted average number of shares of common stock outstanding for the period.

A summary of the Company's calculation of net loss per share is as follows (in thousands except per share amounts):

	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2017</b>	<b>2016</b>	<b>2017</b>	<b>2016</b>
<b>Net loss</b>	<b>\$ (6,933)</b>	<b>\$ (2,675)</b>	<b>\$ (10,021)</b>	<b>\$ (6,783)</b>
Shares used in the calculation of basic and diluted net loss per share	16,424	15,957	16,291	15,896
Effect of dilutive securities:				
Stock options				
Restricted stock				
Diluted shares used in the calculation of net loss per share	16,424	15,957	16,291	15,896
<b>Net loss per share - basic and diluted</b>	<b>\$ (0.42)</b>	<b>\$ (0.17)</b>	<b>\$ (0.62)</b>	<b>\$ (0.43)</b>

The shares of the Company's common stock issuable upon the exercise of stock options and vesting of restricted stock that were excluded from the calculation of diluted net loss per share because their effect would have been antidilutive are as follows:

	<b>Period Ended September 30,</b>	
	<b>2017</b>	<b>2016</b>
Stock options	1,426,513	1,569,166
Restricted stock	507,147	392,148



Stock options and restricted stock	1,933,660	1,961,314
------------------------------------	-----------	-----------

**Note 3 - Business Combinations****Acquisition of VuComp Cancer detection portfolio**

On January 13, 2016, the Company completed the acquisition of the VuCOMP cancer detection portfolio, including the M-Vu computer aided detection (CAD) technology platform. The acquisition includes an extensive library of related clinical data, VuCOMP's key personnel and the customer base that existed at closing of the transaction. The acquisition of the key personnel and clinical data is expected to contribute to the ongoing development of the Company's CAD technology which will be used for future cancer detection research and patents. As the Company considered this to be a business combination, the assets were valued in accordance with ASC Topic 805, *Business Combinations* (ASC 805).

Table of Contents**iCAD, INC. AND SUBSIDIARIES****Notes to Condensed Consolidated Financial Statements****(Unaudited)****September 30, 2017**

The Company acquired VuComp's M-Vu Breast Density product in April 2015. In connection with the diligence of the January 2016 acquisition, VuComp disclosed that it had previously entered into a license agreement pursuant to which it issued an irrevocable, royalty-free worldwide license to a third party. On December 24, 2015, iCAD notified VuComp of a claim under the April 2015 asset purchase agreement based on the disclosure of the third party license agreement, which iCAD believed constituted a breach of VuComp's representation as to its exclusive ownership of its intellectual property at the time of the April 2015 transaction. In connection with the purchase of the VuComp cancer detection portfolio, the Company provided a release of the aforementioned claim. The Company determined that this claim was a component of the purchase price. The Company determined the value of litigation settlement as the excess of the fair value of the business acquired over the cash consideration paid. As a result the Company recorded a gain on litigation settlement of \$249,000 in general and administrative expenses during the first quarter of 2016, which is a component of the purchase price as noted below:

	Amount (000 s)
Cash	\$ 6
Acquisition litigation settlement	249
<b>Purchase price</b>	<b>\$ 255</b>

The amount allocated to the acquired assets was estimated primarily through the use of discounted cash flow valuation techniques. Appraisal assumptions utilized under this method include a forecast of estimated future net cash flows, as well as discounting the future net cash flows to their present value. The following is a summary of the preliminary allocation of the total purchase price based on the estimated fair values as of the date of the acquisition and the amortizable life:

	Amount (000 s)	Estimated amortizable life
Current assets	\$ 84	
Property and equipment	65	3 Years
Identifiable intangible assets	699	1-10 Years
Goodwill	293	
Current liabilities	(280)	
Long-term liabilities	(606)	
<b>Purchase price</b>	<b>\$ 255</b>	

The assets obtained in the acquisition of VuComp's M-Vu Cancer detection portfolio (including the M-Vu breast density product) and the anticipated future revenues are included in the Detection segment and, accordingly, the goodwill resulting from the purchase price allocation is included in goodwill of the Detection segment.

Table of Contents**iCAD, INC. AND SUBSIDIARIES****Notes to Condensed Consolidated Financial Statements****(Unaudited)****September 30, 2017****Note 4 - Sale of MRI Assets**

In December 2016, the Company entered into an Asset Purchase Agreement with Invivo Corporation. In accordance with the agreement, the Company sold to Invivo all right, title and interest to certain intellectual property relating to the Company's VersaVue Software and DynaCAD product and related assets for \$3.2 million. The Company closed the transaction on January 30, 2017 less a holdback reserve of \$350,000 for a net of approximately \$2.9 million. The holdback reserve of \$350,000 has been recorded as an asset in other assets and will be paid to the Company within eighteen months from the closing date, less any amounts, if any, due and payable or reserved under the indemnification provisions in the Asset Purchase agreement.

The Company determined the sale constituted the sale of a business in accordance with ASC 805. The Company performed an evaluation to determine if the sale constituted discontinued operations and concluded that the sale did not represent a major strategic shift, and accordingly it was not considered to be discontinued operations. In connection with the transaction, the Company allocated \$394,000 of goodwill which was a component of the gain on the sale. The allocation was based on the fair value of the assets sold relative to the fair value of the Detection reporting unit as of the date of the agreement, based on the guidance from ASC 350-20-40-3.

The value of the net assets sold is as follows (in thousands):

<b>Assets</b>	
Accounts Receivable	\$ 116
Intangible assets	810
Allocated Goodwill	394
<b>Total Assets</b>	<b>\$ 1,320</b>
<b>Liabilities</b>	
Deferred Revenue	\$ 746
<b>Total Liabilities</b>	<b>\$ 746</b>
<b>Net Assets Sold</b>	<b>\$ 574</b>

In connection with the sale the Company agreed to provide certain transition services to Invivo. The fair value of the transition services were determined based on the cost to provide plus a reasonable profit margin and have been recognized as revenue over the term of approximately ninety days from the closing date. The Company recorded a

gain of \$2.5 million as of January 30, 2017. The components of the gain on the sale are as follows (in thousands):

**Table of Contents****iCAD, INC. AND SUBSIDIARIES****Notes to Condensed Consolidated Financial Statements****(Unaudited)****September 30, 2017**

Gain on Sale	
Cash received	\$ 2,850
Holdback reserve	350
Fair value of transition services	(118)
Net Assets sold	(574)
Total	\$ 2,508

**Note 5 - Inventory**

The components of inventory, net of allowance for obsolete, unmarketable or slow-moving inventories, are summarized as follows (in thousands):

	as of September 30, 2017	as of December 31, 2016
Raw materials	\$ 2,033	\$ 2,503
Work in process	139	75
Finished Goods	1,168	1,149
Inventory	\$ 3,340	\$ 3,727

**Note 6 - Debt financing**

On August 7, 2017 the Company entered into a Loan and Security Agreement (the **Loan Agreement**) with Silicon Valley Bank (the **Bank**) that provides an initial term loan facility (the **Term Loan**) of \$6.0 million and a \$4.0 million revolving line of credit (the **Revolving Loan**). The Company also has the option to secure an additional \$3.0 million under the Loan Agreement for a total of \$9.0 million in 2018, subject to meeting a net revenue minimum of at least \$35.0 million for a trailing twelve month period ending prior to July 30, 2018 (the **Revenue Milestone**).

The Term Loan accrues interest at prime rate. The Company will begin repayment on Sept 1, 2018 in 36 equal monthly installments of principal. Subject to meeting the Revenue Milestone, the Company could elect to defer repayment of the Term Loan to March 1, 2019 in 30 equal monthly payments.

The outstanding Revolving Advances will accrue interest at a floating per annum rate equal to 1.50% above the prime rate for periods when the ratio of the Company's unrestricted cash to the Company's outstanding liabilities to the Bank plus the amount of the Company's total liabilities that mature within one year is at least 1.25 to 1.0. At all other times,

the interest rate shall be 0.50% above the prime rate. The outstanding Term Loan Advances will accrue interest at a floating per annum rate equal to the prime rate.

**Table of Contents****iCAD, INC. AND SUBSIDIARIES****Notes to Condensed Consolidated Financial Statements****(Unaudited)****September 30, 2017**

The maturity date of the Revolving Advances and the Term Loan Advances is August 7, 2021. However, the maturity date will become April 30, 2019, April 30, 2020 or April 30, 2021 if, on or before October 30, 2018, or 2019 or 2020, as applicable, the Company does not agree in writing to the net revenue covenant levels proposed by the Bank with respect to the upcoming applicable calendar year.

If the Revolving Advances are paid in full and the Loan Agreement is terminated prior to the maturity date, then the Company will pay to the Bank a termination fee in an amount equal to two percent (2.0%) of the maximum revolving line of credit. If the Company prepays the Term Loan Advances prior to the maturity date, then the Company will pay to the Bank an amount equal to 1.0%-3.0% of the Term Loan Advances, depending on when such Term Loan Advances are repaid. The Loan Agreement requires the Company to maintain net revenues during the trailing six month period ending on the last day of each calendar quarter as follows: June 30, 2017 - \$10.25 million; September 30, 2017 - \$11.5 million; December 31, 2017 - \$14 million; March 31, 2018 - \$15 million; June 30, 2018 - \$15.25 million; and September 30, 2018 and December 31, 2018 - \$15.5 million. As of September 30, 2017 the Company is in compliance with the revenue covenants in the Loan Agreement.

In connection with the credit line, the Company incurred approximately \$74,000 of closing costs. In accordance with ASU 2015-03 the closing costs have been deducted from the carrying value of the debt and will be amortized over the expected term of 36 months.

The current repayment schedule for the term loan is based on repayment beginning on September 1, 2018. If the Revenue Milestone is met, the Company could elect to defer repayment until March 2019. The carrying value of the Term Loan (net of debt issuance costs) as of September 30, 2017 is as follows (in thousands):

	<b>September 30, 2017</b>
Short-term	\$ 317
Long-term	5,612
<b>Total</b>	<b>\$ 5,929</b>

Interest expense related to the loan for the three and nine month periods ended September 30, 2017 is as follows (in thousands):



	<b>September 30, 2017</b>	
Three months ended	\$	33
Nine month ended		33

**Table of Contents****iCAD, INC. AND SUBSIDIARIES****Notes to Condensed Consolidated Financial Statements****(Unaudited)****September 30, 2017****Note 7 - Lease Commitments****Operating leases**

Facilities are leased under operating leases expiring at various dates through March 2020. Certain of these leases contain renewal options. Rent expense under operating leases was \$229,000 and \$665,000 for the three and nine months ended September 30, 2017, respectively and \$178,000 and \$516,000 for the three and nine months ended September 30, 2016, respectively.

Future minimum lease payments as of September 30, 2017 under operating leases are as follows: (in thousands)

Fiscal Year	Operating Leases
2017	\$ 318
2018	738
2019	746
2020	174
<b>Total</b>	<b>\$ 1,976</b>

**Capital leases**

In August, 2017, the Company assumed an equipment lease obligation with payments totaling \$50,000. The leases were determined to be capital leases and accordingly the equipment was capitalized and a liability of \$42,000 was recorded. The equipment will be depreciated over the expected life of 3 years. Minimum lease payments are as follows (in thousands):

Table of Contents**iCAD, INC. AND SUBSIDIARIES****Notes to Condensed Consolidated Financial Statements****(Unaudited)****September 30, 2017**

Fiscal Year	Capital Lease
2017	4
2018	16
2019	17
2020	13
subtotal minimum lease obligation	50
less interest	(8)
<b>Total, net</b>	<b>42</b>
less current portion	(12)
<b>long term portion</b>	<b>\$ 30</b>

In connection with the Radion/DermEbx Acquisition which closed in July 2014, the Company assumed two separate equipment lease obligations with payments totaling approximately \$2.6 million through May 2017. The leases were determined to be capital leases and accordingly the equipment was capitalized and a liability of \$2.5 million was recorded. In connection with the acquisition, the Company recorded a fair value adjustment to interest expense and amortized the adjustment over the life of the related lease. As of September 30, 2017, there was no further liability for the acquired equipment leases.

**Related Party Lease:**

Kamal Gogineni is an employee of one of the Company's subsidiaries and a stockholder of the Company's common stock. Additionally, Mr. Gogineni is a shareholder of Radion Capital Partners ( RCP ). RCP was the lessor under a lease between RCP and DermEbx (the Lease ). In connection with the Company's acquisition of assets of Radion, Inc. and DermEbx that closed in July 2014, one of the assets and obligations that the Company acquired was the Lease. Pursuant to the Lease, the Company paid approximately \$76,000 to RCP in 2017. As of September 30, 2017, there is no further obligation.

**Note 8 - Stock-Based Compensation**

The Company follows the guidance in ASC Topic 718, *Compensation - Stock Compensation*, ( ASC 718 ).

The Company granted options to purchase 57,352 shares of the Company's stock in the three months ended September 30, 2017. Options granted under the Company's stock incentive plans were valued utilizing the Black-Scholes model using the following assumptions and had the following fair values:



Table of Contents**iCAD, INC. AND SUBSIDIARIES****Notes to Condensed Consolidated Financial Statements****(Unaudited)****September 30, 2017**

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2017</b>	<b>2016</b>	<b>2017</b>	<b>2016</b>
Average risk-free interest rate	1.56%	0.84%	1.52%	0.87%
Expected dividend yield	None	None	None	None
Expected life	3.5 years	3.5 years	3.5 years	3.5 years
Expected volatility	64.2% to 67.0%	68.6% to 75.3%	64.2% to 72.0%	68.6% to 75.3%
Weighted average exercise price	\$4.28	\$5.49	\$4.39	\$5.57
Weighted average fair value	\$2.02	\$2.67	\$2.12	\$2.71

The Company's stock-based compensation expense, including options and restricted stock by category is as follows (in thousands):

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2017</b>	<b>2016</b>	<b>2017</b>	<b>2016</b>
Cost of revenue	\$ 1	\$ 1	5	\$ 5
Engineering and product development	76	82	633	289
Marketing and sales	132	162	854	476
General and administrative	294	201	1,581	878
	\$ 503	\$ 446	\$ 3,073	\$ 1,648

As of September 30, 2017, unrecognized compensation cost (in thousands) related to unexercisable options and unvested restricted stock and the weighted average remaining period is as follows:

Remaining expense	\$ 2,504
Weighted average term	1.1 years

The Company's restricted stock awards typically vest in either one year or three equal annual installments with the first installment vesting one year from grant date. The Company granted a total of 162,500 shares of performance based restricted stock during 2016 with performance measured on meeting a revenue target based on growth for fiscal year 2017 and vesting in three equal installments with the first installment vesting upon measurement of the goal. In addition, a maximum of 108,333 additional shares are available to be earned based on exceeding the revenue goal. Assumptions used to determine the value of performance based grants of restricted stock include the probability of

achievement of the specified revenue targets. Compensation cost for performance based restricted stock requires significant judgment regarding probability of achieving the performance objectives and compensation cost is re-measured at every reporting period. As a result compensation cost could vary significantly during the performance measurement period. The Company granted 153,480 and 392,055 shares of restricted stock with either time based or immediate vesting in the three and nine months ended September 30, 2017, respectively. Included in the restricted shares granted in the second quarter of 2017 are 172,668 shares that were issued in lieu of cash bonus payments and was approved by the Board of Directors in February 2017. The number of shares granted were determined based the amount of approved bonus divided by the stock price of the Company at the date of issuance.

**Table of Contents****iCAD, INC. AND SUBSIDIARIES****Notes to Condensed Consolidated Financial Statements****(Unaudited)****September 30, 2017**

The Company's aggregate intrinsic value for stock options and restricted stock outstanding is as follows (in thousands):

	<b>Period Ended September 30,</b>	
	<b>2017</b>	<b>2016</b>
Aggregate intrinsic value		
Stock options	\$ 1,050	\$ 1,748
Restricted stock	2,242	2,039

The intrinsic value of stock options exercised during the three and nine months ended September 30, 2017 was \$12,000 and \$50,000, respectively. The intrinsic value of stock options exercised during the three and nine months September 30, 2016 was \$189,000 and \$195,000, respectively. The intrinsic value of restricted shares that vested in the three and nine months ended September 30, 2017 was \$0.2 million and \$1.7 million, respectively. The intrinsic value of restricted shares that vested in the three and nine months ended September 30, 2016 was \$0.0 million and \$1.0 million, respectively.

**Note 9 - Commitments and Contingencies****Foreign Tax Claim**

In July 2007, a dissolved former Canadian subsidiary of the Company, CADx Medical Systems Inc. ( CADx Medical ), received a tax re-assessment of approximately \$6,800,000 from the Canada Revenue Agency ( CRA ) resulting from CRA's audit of CADx Medical's Canadian federal tax return for the year ended December 31, 2002. In February 2010 the CRA reviewed the matter and reduced the tax re-assessment to approximately \$703,000, excluding interest and penalties. The Company believes that it is not liable for the re-assessment against CADx Medical and no accrual has been recorded for this matter as of September 30, 2017.

**Settlement Obligations**

In connection with the acquisition of Xoft in 2010, the Company recorded a royalty obligation pursuant to a settlement agreement entered into between Xoft and Hologic in August 2007. Xoft received a nonexclusive, irrevocable, perpetual, worldwide license, including the right to sublicense certain Hologic patents, and a non-compete covenant as well as an agreement not to seek further damages with respect to the alleged patent violations. In return, the Company had a remaining obligation to pay a minimum annual royalty payment to Hologic, of \$250,000 payable through 2016. In addition to the minimum annual royalty payments, the litigation settlement agreement with Hologic also provided for payment of royalties based upon a specified percentage of future net sales on





**Table of Contents**

**iCAD, INC. AND SUBSIDIARIES**

**Notes to Condensed Consolidated Financial Statements**

**(Unaudited)**

**September 30, 2017**

any products that utilize the licensed rights. The Company has a liability within accounts payable and accrued expenses for future payment and for the remaining minimum royalty obligations totaling \$448,000 as of September 30, 2017. The Company recorded interest expense of approximately \$10,000 and \$30,000 in the three and nine months September 30, 2016, respectively, related to this obligation.

In December, 2011, the Company agreed to a settlement related to litigation with Carl Zeiss Meditec AG. In July 2017, the Company paid the remaining \$500,000 due and there is no further obligation to Zeiss. The Company recorded interest expense of approximately \$0 and \$26,000 in the three and nine months ended September 30, 2017, respectively and \$13,000 and \$39,000 in the three and nine months ended September 30, 2016, respectively related to this obligation.

**Other Commitments**

The Company is obligated to pay approximately \$0.8 million for firm purchase obligations to suppliers for future product and service deliverables.

**Litigation**

The Company is a party to various legal proceedings and claims arising out of the ordinary course of its business. Although the final results of all such matters and claims cannot be predicted with certainty, the Company currently believes that there are no current proceedings or claims pending against it the ultimate resolution of which would have a material adverse effect on its financial condition or results of operations. However, should the Company fail to prevail in any legal matter or should several legal matters be resolved against the Company in the same reporting period, such matters could have a material adverse effect on our operating results and cash flows for that particular period. In all cases, at each reporting period, the Company evaluates whether or not a potential loss amount or a potential range of loss is probable and reasonably estimable under ASC 450, Contingencies. Legal costs are expensed as incurred.

**Note 10 - Fair Value Measurements**

The Company follows the provisions of ASC Topic 820, *Fair Value Measurement and Disclosures*, (ASC 820). This topic defines fair value, establishes a framework for measuring fair value under US GAAP and enhances disclosures about fair value measurements. Fair value is defined under ASC 820 as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value under ASC 820 must maximize the use of observable inputs and minimize the use of unobservable inputs. The standard describes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value which are the following:



Table of Contents**iCAD, INC. AND SUBSIDIARIES****Notes to Condensed Consolidated Financial Statements****(Unaudited)****September 30, 2017**

Level 1 - Quoted prices in active markets for identical assets or liabilities.

Level 2 - Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 - Unobservable inputs that are supported by little or no market activity and that are significant to the fair value.

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.

Our financial instruments include cash and cash equivalents, accounts receivable, accounts payable certain accrued liabilities and debt. The carrying amounts of our cash and cash equivalents (which are composed primarily of deposit and overnight sweep accounts), accounts receivable, accounts payable and certain accrued liabilities approximate fair value due to the short maturity of these instruments. The carrying value of our term loan approximates fair value due to the market rate of the stated interest rate.

The Company's assets that are measured at fair value on a recurring basis relate to the Company's money market accounts.

The Company's money market funds are included in cash and cash equivalents in the accompanying balance sheets and are considered a Level 1 investment as they are valued at quoted market prices in active markets.

The following table sets forth the Company's assets and liabilities which are measured at fair value on a recurring basis by level within the fair value hierarchy.

**Fair value measurements using: (000 \$) as of December 31, 2016**

	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total</b>
<b>Assets</b>				
Money market accounts	\$ 6,622	\$	\$	\$ 6,622
<b>Total Assets</b>	<b>\$ 6,622</b>	<b>\$</b>	<b>\$</b>	<b>\$ 6,622</b>

**Fair value measurements using: (000 s) as of September 30, 2017**

	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total</b>
<b>Assets</b>				
Money market accounts	\$ 10,054	\$	\$	\$ 10,054
<b>Total Assets</b>	<b>\$ 10,054</b>	<b>\$</b>	<b>\$</b>	<b>\$ 10,054</b>

Table of Contents**iCAD, INC. AND SUBSIDIARIES****Notes to Condensed Consolidated Financial Statements****(Unaudited)****September 30, 2017***Items Measured at Fair Value on a Nonrecurring Basis*

Certain assets, including long-lived assets and goodwill, are measured at fair value on a nonrecurring basis. These assets are recognized at fair value when they are deemed to be impaired. The Company recorded a \$4.7 million impairment in the quarter ended September 30, 2017 which consisted of \$4.0 million related to goodwill and \$0.7 million related to long-lived assets as discussed in Note 12 and Note 13 and remeasured long-lived assets and goodwill of the Therapy reporting unit at fair value as of the impairment date as noted in the following table. The fair values of long-lived assets and goodwill were measured using Level 3 inputs.

**Fair value measurements using: (000 s) as of September 30, 2017**

	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total</b>
Non-recurring assets				
Long-lived and intangible assets	\$	\$	\$ 780	\$ 780
Goodwill			1,766	1,766
Total Assets	\$	\$	\$ 2,546	\$ 2,546

**Note 11 - Income Taxes**

The Company recorded an income tax benefit of \$42,000 and \$28,000 for the three and nine months ended September 30, 2017, respectively, as compared to a provision of \$10,000 and \$55,000 for the three and nine months ended September 30, 2016, respectively. The tax benefit for the three and nine months ended September 30, 2017 is the result of applying for research and development credits in New Hampshire. In the second quarter of 2017, the Company applied for \$50,000 of research and development credits from New Hampshire. The Company anticipates the credits to be allocated for the 2016 tax year as well as the 2017 tax year. The research and development credits have been utilized to decrease the New Hampshire non-income tax liability to zero. The \$42,000 benefit for the quarter is a result of the utilization of these credits and the decrease of the overall state tax.. At September 30, 2017, the Company had no material unrecognized tax benefits and a deferred tax liability of \$12,400 related to tax amortizable goodwill. The Company recorded a deferred tax liability of approximately \$1,900 through September 30, 2017. No other adjustments were required under ASC 740, *Income Taxes*. The Company does not expect that the unrecognized tax benefits will materially increase within the next 12 months. The Company did not recognize any interest or penalties related to uncertain tax positions at September 30, 2017.

On January 1, 2017, the Company adopted the Financial Accounting Standards Board ( FASB ) Accounting Standards Update ( ASU ) No. 2016-09, *Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting* ( ASU 2016-09 ). Under ASU 2016-09, excess tax benefits and tax deficiencies are

recognized as income tax expense or benefit in the income statement, and excess tax benefits are recognized regardless of whether the benefit reduces taxes payable in the current period. The tax effects of exercised or vested awards are treated as discrete items in the reporting period in which they occur. As a result of the adoption, the net operating loss deferred tax assets increased by \$2.1 million and are offset by a corresponding increase in the valuation allowance. The Company files United States federal income tax returns and

**Table of Contents**

**iCAD, INC. AND SUBSIDIARIES**

**Notes to Condensed Consolidated Financial Statements**

**(Unaudited)**

**September 30, 2017**

income tax returns in various states and local jurisdictions. The Company's three preceding tax years remain subject to examination by federal and state taxing authorities. In addition, because the Company has net operating loss carry-forwards, the Internal Revenue Service and state jurisdictions are permitted to audit earlier years and propose adjustments up to the amount of net operating loss generated in those years. The Company is not currently under examination by any federal or state jurisdiction for any tax years.

**Note 12 - Goodwill**

In accordance with FASB ASC Topic 350-20, *Intangibles - Goodwill and Other*, (ASC 350-20), the Company tests goodwill for impairment on an annual basis and between annual tests if events and circumstances indicate it is more likely than not that the fair value of the reporting unit is less than the carrying value of the reporting unit. The Company's annual test date is October 1 of each year.

Factors the Company considers important, which could trigger an impairment of such asset, include the following:

significant underperformance relative to historical or projected future operating results;

significant changes in the manner or use of the assets or the strategy for the Company's overall business;

significant negative industry or economic trends;

significant decline in the Company's stock price for a sustained period; and

a decline in the Company's market capitalization below net book value.

The Company would record an impairment charge if such an assessment were to indicate that the fair value of a reporting unit was less than the carrying value. In evaluating potential impairments outside of the annual measurement date, judgment is required in determining whether an event has occurred that may impair the value of goodwill or intangible assets. The Company utilizes either discounted cash flow models or other valuation models, such as comparative transactions and market multiples, to determine the fair value of reporting units. The Company makes assumptions about future cash flows, future operating plans, discount rates, comparable companies, market multiples, purchase price premiums and other factors in those models. Different assumptions and judgment determinations could

yield different conclusions that would result in an impairment charge to income in the period that such change or determination was made.

As a result of the underperformance of the Therapy reporting unit as compared to expected future results, the Company determined there was a triggering event in the third quarter of 2017. As a result, the Company completed an interim impairment assessment. The interim test resulted in the fair value of the Therapy reporting unit being less than the carrying value of the reporting unit. The Company did not identify a triggering event within the Detection reporting unit and accordingly did not perform an interim test.



**Table of Contents**

**iCAD, INC. AND SUBSIDIARIES**

**Notes to Condensed Consolidated Financial Statements**

**(Unaudited)**

**September 30, 2017**

The Company elected to early adopt ASU 2017-04, Intangibles – Goodwill and Other: Simplifying the Test for Goodwill Impairment ( ASU 2017-04 ). ASU 2017-04 specifies that goodwill impairment is the amount by which a reporting unit's carrying value exceeds its fair value, not to exceed the carrying amount of goodwill. In accordance with the standard, the fair value of the Therapy reporting unit was \$3.5 million and the carrying value was \$7.5 million. The deficiency of \$4.0 million was recorded as an impairment charge in the quarter ended September 30, 2017.

The carrying values of the reporting units were determined based on an allocation of our assets and liabilities through specific allocation of certain assets and liabilities to the reporting units and an apportionment of the remaining net assets based on the relative size of the reporting units' revenues and operating expenses compared to the Company as a whole. The determination of reporting units also requires management judgment.

The Company determined the fair values for each reporting unit using a weighting of the income approach and the market approach. For purposes of the income approach, fair value is determined based on the present value of estimated future cash flows, discounted at an appropriate risk adjusted rate. The Company used internal forecasts to estimate future cash flows and includes an estimate of long-term future growth rates based on the most recent views of the long-term forecast for each segment. Accordingly, actual results can differ from those assumed in the forecasts. The discount rate of approximately 18% is derived from a capital asset pricing model and analyzing published rates for industries relevant to the reporting units to estimate the cost of equity financing. The Company uses discount rates that are commensurate with the risks and uncertainty inherent in the respective businesses and in the internally developed forecasts.

In the market approach, the Company uses a valuation technique in which values are derived based on market prices of publicly traded companies with similar operating characteristics and industries. A market approach allows for comparison to actual market transactions and multiples. It can be somewhat limited in its application because the population of potential comparable publicly-traded companies can be limited due to differing characteristics of the comparative business and ours, as well as market data may not be available for divisions within larger conglomerates or non-public subsidiaries that could otherwise qualify as comparable, and the specific circumstances surrounding a market transaction (e.g., synergies between the parties, terms and conditions of the transaction, etc.) may be different or irrelevant with respect to the business.

The Company corroborated the total fair values of the reporting units using a market capitalization approach; however, this approach cannot be used to determine the fair value of each reporting unit value. The blend of the income approach and market approach is more closely aligned to the business profile of the Company, including markets served and products available. In addition, required rates of return, along with uncertainties inherent in the forecast of future cash flows, are reflected in the selection of the discount rate. In addition, under the blended approach, reasonably likely scenarios and associated



**Table of Contents****iCAD, INC. AND SUBSIDIARIES****Notes to Condensed Consolidated Financial Statements****(Unaudited)****September 30, 2017**

sensitivities can be developed for alternative future states that may not be reflected in an observable market price. The Company will assess each valuation methodology based upon the relevance and availability of the data at the time the valuation is performed and weight the methodologies appropriately.

As discussed in Note 3, in April 2015, the Company acquired VuComp's M-V<sup>®</sup> Breast Density product for \$1.7 million. The product was integrated into the Company's Powerlook AMP system, which is a component of the Detection reporting unit. The Company determined that the acquisition was a business combination and recorded goodwill of \$0.8 million to the Detection segment. In January 2016, the Company completed the acquisition of VuComp's M-Vu CAD and other assets for \$6,000. The customers, related technology and clinical data acquired are being used for the Company's Cancer Detection products and the Company recorded goodwill of \$293,000 to the Detection segment.

In December 2016, the Company entered into an Asset Purchase Agreement with Invivo Corporation. The Company sold and conveyed to Buyer all right, title and interest to certain intellectual property relating to the VersaVue Software and the DynaCAD product and related assets. As a result of the Asset Purchase Agreement, the Company determined that the sale constituted the sale of a business and the Company allocated \$394,000 of goodwill to assets held for sale as of December 31, 2016. The allocation was based on the fair value of the assets sold relative to the fair value of the Detection reporting unit as of the date of the Asset Purchase Agreement. The Company closed the transaction on January 30, 2017, and goodwill was a component of the net assets sold as of the closing date.

A roll forward of goodwill activity by reportable segment is as follows (in thousands):

	Detection	Therapy	Total
Balance at December 31, 2016	8,362	5,735	14,097
Impairment		(3,969)	(3,969)
Balance at September 30, 2017	\$ 8,362	\$ 1,766	\$ 10,128
Accumulated Goodwill	699	6,270	54,906
Fair value allocation	7,663	13,446	
Accumulated impairment		(17,950)	(44,778)
Balance at September 30, 2017	\$ 8,362	\$ 1,766	\$ 10,128

**Note 13 - Long-lived assets**

In accordance with FASB ASC Topic 360, Property, Plant and Equipment (ASC 360), the Company assesses long-lived assets for impairment if events and circumstances indicate it is more likely than not that the fair value of the asset group is less than the carrying value of the asset group.

---

**Table of Contents**

**iCAD, INC. AND SUBSIDIARIES**

**Notes to Condensed Consolidated Financial Statements**

**(Unaudited)**

**September 30, 2017**

ASC 360-10-35 uses events and circumstances criteria to determine when, if at all, an asset (or asset group) is evaluated for recoverability. Thus, there is no set interval or frequency for recoverability evaluation. In accordance with ASC 360-10-35-21 the following factors are examples of events or changes in circumstances that indicate the carrying amount of an asset (asset group) may not be recoverable and thus is to be evaluated for recoverability.

A significant decrease in the market price of a long-lived asset (asset group);

A significant adverse change in the extent or manner in which a long-lived asset (asset group) is being used or in its physical condition;

A significant adverse change in legal factors or in the business climate that could affect the value of a long-lived asset (asset group), including an adverse action or assessment by a regulator;

An accumulation of costs significantly in excess of the amount originally expected for the acquisition or construction of a long-lived asset (asset group);

A current period operating or cash flow loss combined with a history of operating or cash flow losses or a projection or forecast that demonstrates continuing losses associated with the use of a long-lived asset (asset group).

In accordance with ASC 360-10-35-17, if the carrying amount of an asset or asset group (in use or under development) is evaluated and found not to be fully recoverable (the carrying amount exceeds the estimated gross, undiscounted cash flows from use and disposition), then an impairment loss must be recognized. The impairment loss is measured as the excess of the carrying amount over the assets (or asset group's) fair value.

The Company completed an interim goodwill impairment assessment for the Therapy reporting unit and noted that there was a goodwill impairment (see Note 13). As a result, the Company determined this was a triggering event for long-lived assets. Accordingly, the Company completed an analysis pursuant to ASC 360-10-35-17 and determined that the carrying value of the asset group exceeded the undiscounted cash flows, and that long-lived assets were impaired. The Company recorded long-lived asset impairment charges of approximately \$0.7 million in the third quarter ended September 30, 2017 based on the deficiency between the book value of the assets and the fair value as determined in the analysis. At September 30, 2017, the long lived assets in the asset group are recorded at their current fair values.

A considerable amount of judgment and assumptions are required in performing the impairment tests, principally in determining the fair value of the asset group and the reporting unit. While the Company believes the judgments and assumptions are reasonable, different assumptions could change the estimated fair values and, therefore additional impairment charges could be required. Significant negative industry or economic trends, disruptions to the Company's business, loss of significant customers, inability to effectively integrate acquired businesses, unexpected significant changes or planned changes in use of the assets may adversely impact the assumptions used in the fair value estimates and ultimately result in future impairment charges.

**Table of Contents**

**iCAD, INC. AND SUBSIDIARIES**

**Notes to Condensed Consolidated Financial Statements**

**(Unaudited)**

**September 30, 2017**

**Note 14 - Segment Reporting**

In accordance with FASB Topic ASC 280, *Segments*, operating segments, are defined as components of an enterprise that engage in business activities for which discrete financial information is available and regularly reviewed by the chief operating decision maker ( CODM ) in deciding how to allocate resources and assess performance.

The Company's CODM is the CEO. Each segment generates revenue from the sale of medical equipment and related services and/or sale of supplies. The Company has determined there are two segments, Cancer Detection and Cancer Therapy.

The Detection segment consists of our advanced image analysis and workflow products, and the Therapy segment consists of our radiation therapy Axxent products, and related services. The primary factors used by our CODM to allocate resources are based on revenues, gross profit, operating income, and earnings or loss before interest, taxes, depreciation, amortization, and other specific and non-recurring items ( Adjusted EBITDA ) of each segment. Included in segment operating income are stock compensation, amortization of technology and depreciation expense. There are no intersegment revenues.

Our CODM does not use asset information by segment to allocate resources or make operating decisions.

Table of Contents**iCAD, INC. AND SUBSIDIARIES****Notes to Condensed Consolidated Financial Statements****(Unaudited)****September 30, 2017**

Segment revenues, gross profit, segment operating income or loss, and a reconciliation of segment operating income or loss to GAAP loss before income tax is as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
<b>Segment revenues:</b>				
Detection	\$ 4,346	\$ 4,134	\$ 13,066	\$ 12,961
Therapy	2,654	1,869	7,134	6,449
Total Revenue	\$ 7,000	\$ 6,003	\$ 20,200	\$ 19,410
<b>Segment gross profit:</b>				
Detection	\$ 3,822	\$ 3,586	\$ 11,553	\$ 11,429
Therapy	821	515	2,282	2,560
Segment gross profit	\$ 4,643	\$ 4,101	\$ 13,835	\$ 13,989
<b>Segment operating income (loss):</b>				
Detection	1,475	1,250	4,261	4,494
Therapy	(6,451)	(2,055)	(10,627)	(5,398)
Segment operating income (loss)	\$ (4,976)	\$ (805)	\$ (6,366)	\$ (904)
<b>General, administrative, depreciation and amortization expense</b>				
General, administrative, depreciation and amortization expense	\$ (1,966)	\$ (1,847)	\$ (6,143)	\$ (5,774)
Interest expense	(36)	(15)	(51)	(59)
Gain on sale of MRI assets			2,508	
Other income	3	2	3	9
Loss before income tax	\$ (6,975)	\$ (2,665)	\$ (10,049)	\$ (6,728)

**Note 15 - Recent Accounting Pronouncements**

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606), or ASU 2014-09, which superseded nearly all existing revenue recognition guidance under U.S. GAAP. Since then, the FASB



has also issued ASU 2016-08, Revenue from Contracts with Customers (Topic 606), Principals versus Agent Considerations and ASU 2016-10, Revenue from Contracts with Customers (Topic 606), Identifying Performance Obligations and Licensing, which further elaborate on the original ASU No. 2014-09. The core principle of these updates is to recognize revenue when promised goods or services are transferred to customers in an amount that reflects the consideration to which the entity expects to be entitled for those goods or services. ASU 2014-09 defines a five step process to achieve this core principle and, in doing so, more judgments and estimates may be required within the revenue recognition process than are required under existing U.S. GAAP. In July 2015, the FASB approved a one-year deferral of the effective date to January 1, 2018, with early adoption to be permitted as of the original effective date of January 1, 2017. Once this standard becomes effective, companies may use either of the following transition methods: (i) a full retrospective approach

**Table of Contents**

**iCAD, INC. AND SUBSIDIARIES**

**Notes to Condensed Consolidated Financial Statements**

**(Unaudited)**

**September 30, 2017**

reflecting the application of the standard in each reporting period with the option to elect certain practical expedients, or (ii) a retrospective approach with the cumulative effect of initially adopting ASU 2014-09 recognized at the date of adoption (which includes additional footnote disclosures).

The Company has performed an assessment of its revenue streams and customer classes. The Company has used this information to develop an implementation plan which it expects to complete during the fourth quarter of 2017. The Company does not expect that its revenue recognition will be materially impacted by the new guidance. The Company is also assessing the impact of the guidance on its contract costs in order to determine the magnitude of impact. The Company currently expects to adopt the guidance using the modified retrospective approach, and will finalize this selection along with completion of the implementation plan.

There are also certain considerations related to internal control over financial reporting that are associated with implementing Topic 606. The Company is evaluating its internal control framework over revenue recognition to identify any changes that may need to be made in relation to the implementation process, as well as upon adoption of the new guidance.

In addition, disclosure requirements under the new guidance in Topic 606 have been significantly expanded in comparison to the disclosure requirements under the current guidance. The Company's implementation phase includes designing and implementing the appropriate internal controls to obtain and disclose the information required under Topic 606.

The Company expects to adopt certain practical expedients and make certain policy elections related to the accounting for significant finance components, sales taxes, shipping and handling, costs to obtain a contract and immaterial promised goods or services, which will mitigate certain impacts of adopting Topic 606. The Company also expects to review the tax impact, if any, that Topic 606 will have on the financial statements.

In February 2016, the FASB issued ASU No. 2016-02, *Leases*. The standard establishes a right-of-use ( ROU ) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. The new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. We are currently evaluating the impact of our pending adoption of the new standard on our consolidated financial statements, however the adoption of the standard is expected to increase both assets and liabilities for leases that would previously have been off-balance sheet operating leases.



**Table of Contents**

**iCAD, INC. AND SUBSIDIARIES**

**Notes to Condensed Consolidated Financial Statements**

**(Unaudited)**

**September 30, 2017**

On January 1, 2017, we adopted the Financial Accounting Standards Board ( FASB ) Accounting Standards Update ( ASU ) No. 2016-09, Compensation Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting ( ASU 2016-09 ), which simplifies several aspects of the accounting for employee share-based payment transactions, including income taxes consequences, classification of awards as either equity or liabilities, and classification in the statement of cash flows. Under ASU 2016-09, excess tax benefits and tax deficiencies are recognized as income tax expense or benefit in the income statement, and excess tax benefits are recognized regardless of whether the benefit reduces taxes payable in the current period. The tax effects of exercised or vested awards are treated as discrete items in the reporting period in which they occur. As a result of the adoption, the net operating loss deferred tax assets increased by \$2.1 million and are offset by a corresponding increase in the valuation allowance.

In August 2016, the FASB issued ASU 2016-15, Statement of Cash Flows (Topic 230) , a consensus of the FASB s Emerging Issues Task Force. This update is intended to reduce diversity in practice in how certain transactions are classified in the statement of cash flows. The update requires cash payments for debt prepayment or debt extinguishment costs to be classified as cash outflows for financing activities. It also requires cash payments made soon after an acquisition s consummation date (approximately three months or less) to be classified as cash outflows for investing activities. Payments made thereafter should be classified as cash outflows for financing activities up to the amount of the original contingent consideration liability. Payments made in excess of the amount of the original contingent consideration liability should be classified as cash outflows for operating activities. The amendment is effective for annual periods beginning after December 15, 2017, and interim periods thereafter. Early adoption is permitted. The Company does not expect the adoption of this amendment will have a material impact on our consolidated financial statements.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

Safe Harbor Statement under the Private Securities Litigation Reform Act of 1995: Certain information included in this Item 2 and elsewhere in this Form 10-Q that are not historical facts contain forward looking statements that involve a number of known and unknown risks, uncertainties and other factors that could cause the actual results, performance or achievements of the Company to be materially different from any future results, performance or achievement expressed or implied by such forward looking statements. These risks and uncertainties include, but are not limited to, uncertainty of future sales and expense levels, protection of patents and other proprietary rights, the impact of supply and manufacturing constraints or difficulties, regulatory changes and requirements applicable to our products, product market acceptance, possible technological obsolescence of products, increased competition, integration of the acquired businesses, the impact of litigation and/or government regulation, changes in Medicare reimbursement policies, competitive factors, the effects of a decline in the economy in markets served by the Company and other risks detailed in the Company's other filings with the Securities and Exchange Commission. The words believe, plan, intend, expect, estimate, anticipate, likely, seek, should, would, could and identify forward-looking statements. Readers are cautioned not to place undue reliance on those forward-looking statements, which speak only as of the date the statement was made.

**Results of Operations****Overview**

iCAD delivers innovative cancer detection and radiation therapy solutions and services that enable clinicians to find and treat cancers earlier and while enhancing patient care. iCAD offers a comprehensive range of upgradeable computer aided detection (CAD) and workflow solutions to support rapid and accurate detection of breast and colorectal cancers. iCAD's Xoft Axxent<sup>®</sup> Electronic Brachytherapy (eBx<sup>®</sup>) System<sup>®</sup> is a painless, non-invasive technology that delivers high dose rate, low energy radiation, which targets cancer while minimizing exposure to surrounding healthy tissue. The Xoft System is FDA cleared and CE marked for use anywhere in the body, including treatment of non-melanoma skin cancer, early-stage breast cancer and gynecological cancers. The comprehensive iCAD technology platforms include advanced hardware and software as well as management services designed to support cancer detection and radiation therapy treatments.

The Company has grown primarily through acquisitions including CADx, Qualia Computing, CAD Sciences, Xoft, DermEbx, Radion and VuComp. The Radion/DermEbx acquisition extended the Company's position as a larger player in the oncology market, including the components that enable dermatologists and radiation oncologists to develop, launch and manage their electronic brachytherapy (eBx) programs for the treatment of non-melanoma skin cancer (NMSC). The VuComp acquisition included an extensive library of related clinical data which we use for cancer detection research and patents, as well as key personnel and expanded our customer base.

---

**Table of Contents**

In the Detection segment, our industry-leading solutions include advanced image analysis and workflow solutions that enable healthcare professionals to better serve patients by identifying pathologies and pinpointing the most prevalent cancers earlier, a comprehensive range of high-performance, upgradeable Computer-Aided Detection (CAD) systems and workflow solutions for mammography, Magnetic Resonance Imaging (MRI) and Computed Tomography (CT).

The Company intends to continue the extension of its image analysis and clinical decision support solutions for mammography and CT imaging. The Company believes that advances in digital imaging techniques, such as 3D mammography, should bolster its efforts to develop additional commercially viable CAD/advanced image analysis and workflow products. In January 2016, the Company completed the acquisition of VuComp's M-Vu cancer detection portfolio including M-Vu CAD for \$6,000. The acquisition provided clinical data for research and an additional customer install base to sell the Company's cancer detection solutions. In December 2016, the Company entered into an Asset Purchase Agreement with Invivo Corporation. The Company sold and conveyed to Invivo all right, title and interest to certain intellectual property relating to the VersaVue Software and the DynaCAD product and related assets. The Company closed the transaction on January 30, 2017, and recorded a gain on the sale of approximately \$2.5 million as of the closing date. In March 2017, the Company announced that it received Premarket Approval from the U.S. Food and Drug Administration (the FDA) for the Powerlook Tomo Detection product.

In the Therapy segment, the Company offers an isotope-free cancer treatment platform technology. The Xoft Electronic Brachytherapy System (Xoft eBx) can be used for the treatment of early-stage breast cancer, endometrial cancer, cervical cancer and skin cancer. We believe the Xoft eBx system platform indications represent strategic opportunities in the United States and international markets to offer differentiated treatment alternatives. In addition, the Xoft eBx system generates additional recurring revenue for the sale of consumables and related accessories and offer solutions that enable dermatologists and radiation oncologists to develop, launch and manage their eBx programs for the treatment of NMSC.

As we have discussed in our risk factors noted in our Annual Report on Form 10-K filed with the SEC for the year ended December 31, 2016, our business can be affected by coverage policies adopted by federal and state governmental authorities, such as Medicare and Medicaid, as well as private payers, which often follow the coverage policies of these public programs. Such policies may affect which products customers purchase and the prices customers are willing to pay for those products in a particular jurisdiction.

The Company's headquarters are located in Nashua, New Hampshire, with a manufacturing facility in New Hampshire and an operations, research, development, manufacturing and warehousing facility in San Jose, California.

**Critical Accounting Policies**

The Company's discussion and analysis of its financial condition, results of operations, and cash flows are based on the Company's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The

**Table of Contents**

preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, the Company evaluates these estimates, including those related to accounts receivable allowance, inventory valuation and obsolescence, intangible assets, income taxes, warranty obligations, contingencies and litigation. Additionally, the Company uses assumptions and estimates in calculations to determine stock-based compensation. The Company bases its estimates on historical experience and on various other assumptions that it believes to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. For a comprehensive list of the Company's critical accounting policies, reference should be made to the Annual Report on Form 10-K for the year ended December 31, 2016 filed on March 24, 2017.

**Table of Contents****Three months ended September 30, 2017 compared to the three months ended September 30, 2016****Revenue: (in thousands)**

	<b>Three months ended September 30,</b>			
	<b>2017</b>	<b>2016</b>	<b>Change</b>	<b>% Change</b>
<b>Detection revenue</b>				
Product revenue	\$ 2,758	\$ 1,991	\$ 767	38.5%
Service revenue	1,588	2,143	(555)	(25.9)%
Subtotal	4,346	4,134	212	5.1%
<b>Therapy revenue</b>				
Product revenue	668	23	645	2804.3%
Service revenue	1,986	1,846	140	7.6%
Subtotal	2,654	1,869	785	42.0%
<b>Total revenue</b>	<b>\$ 7,000</b>	<b>\$ 6,003</b>	<b>\$ 997</b>	<b>16.6%</b>

*Three months ended September 30, 2017 and 2016:*

Total revenue for the three month period ended September 30, 2017 was \$7.0 million compared with revenue of \$6.0 million for the three month period ended September 30, 2016, an increase of approximately \$1.0 million, or 16.6%. The increase in revenue was due to increases in Detection revenues of approximately \$0.2 million and an increase in Therapy revenue of approximately \$0.8 million.

Detection product revenue increased by approximately \$0.8 million from \$2.0 million to \$2.8 million or 38.5% in the three months ended September 30, 2017 as compared to the three months ended September 30, 2016. The increase is due primarily to an increase in digital systems driven by increases in sales to our OEM partners.

Detection service and supplies revenue decreased by approximately \$0.6 million from \$2.1 million in the three months ended September 30, 2016 to \$1.6 million in the three months ended September 30, 2017. The decrease in service and supplies revenue is due primarily to the decrease in service revenue associated with the MRI business. Service and supplies revenue reflects the sale of service contracts to our installed base of customers. Service and supplies revenue related to our installed base of customers can vary from quarter to quarter.

Therapy product revenue was approximately \$0.7 million for the three months ended September 30, 2017 as compared to \$23,000 for the three months ended September 30, 2016. The increase in product revenue for the quarter ended September 30, 2017 is due to the sale of Axxent eBx systems in the quarter. Product revenue from the sale of our Axxent eBx systems can vary significantly due to an increase or decrease in the number of units sold which can cause a significant fluctuation in product revenue in the period.

Therapy service and supply revenue was approximately \$2.0 million for the three months ended





**Table of Contents**

September 30, 2017 as compared to \$1.9 million for the three months ended September 30, 2016. Therapy service and supplies revenue is primarily the services related to electronic brachytherapy for non-melanoma skin cancer ( NMSC ).

**Cost of Revenue and Gross Profit: (in thousands)**

	<b>Three months ended September 30,</b>			
	<b>2017</b>	<b>2016</b>	<b>Change</b>	<b>% Change</b>
Products	\$ 636	\$ 236	\$ 400	169.5%
Service and supplies	1,458	1,370	88	6.4%
Amortization and depreciation	263	296	(33)	(11.1)%
Total cost of revenue	\$ 2,357	\$ 1,902	\$ 455	23.9%
Gross profit	\$ 4,643	\$ 4,101	\$ 542	13.2%
Gross profit %	66.3%	68.3%		(2.0)%
	<b>Three months ended September 30,</b>			
	<b>2017</b>	<b>2016</b>	<b>Change</b>	<b>% Change</b>
Detection gross profit	\$ 3,822	\$ 3,586	\$ 236	6.6%
Therapy gross profit	821	515	306	59.4%
Gross profit	\$ 4,643	\$ 4,101	\$ 542	13.2%

Gross profit for the three month period ended September 30, 2017 was \$4.6 million, or 66.3% of revenue as compared to \$4.1 million or 68.3% of revenue in the three month period ended September 30, 2016. Gross profit percent changes are primarily due to changes in the mix of business, consulting costs related to non-recurring engineering revenue, additional manufacturing investments and amortization of acquired intangibles.

Cost of products increased by approximately \$0.4 million from approximately \$0.2 million for the three months ended September 30, 2016 to approximately \$0.6 million for the three months ended September 30, 2017. The increase is due primarily the increase in therapy product revenue for the third quarter of 2017. The cost of product revenue as a percentage of product revenue was approximately 19% for the three months ended September 30, 2017 as compared to 12% for the three months ended September 30, 2016. The increase in cost of product revenue as a percentage of product revenue is due primarily to the sale of Axxent eBx controllers which have a higher cost of revenue than Detection products.

The cost of service and supplies was \$1.5 million for the three months ended September 30, 2017 as compared to \$1.4 million for the three months ended September 30, 2016. The cost of service and supplies revenue as a percentage of service and supplies revenue was approximately 41% for the quarter ended September 30, 2017 and 34% for the quarter ended September 30, 2016.

**Table of Contents**

Amortization and depreciation was approximately \$0.3 million in each of the three month periods ended September 30, 2016 and September 30, 2017.

**Operating Expenses: (in thousands)**

	<b>Three months ended September 30,</b>			
	2017	2016	Change	Change %
<b>Operating expenses:</b>				
Engineering and product development	\$ 2,254	\$ 2,360	\$ (106)	(4.5)%
Marketing and sales	2,580	2,322	258	11.1%
General and administrative	1,944	1,783	161	9.0%
Amortization and depreciation	107	288	(181)	(62.8)%
Goodwill and long-lived asset impairment	4,700		4,700	0.0%
<b>Total operating expenses</b>	<b>\$ 11,585</b>	<b>\$ 6,753</b>	<b>\$ 4,832</b>	<b>71.6%</b>

Operating expenses increased by approximately \$4.8 million or 71.6% in the three months ended September 30, 2017. The increase is due primarily to the goodwill and long lived asset impairment of \$4.7 million.

*Engineering and Product Development.* Engineering and product development costs were approximately \$2.3 million for the three month period ended September 30, 2017 as compared to \$2.4 million for the three month periods ended September 30, 2016. Detection engineering and product development costs were \$1.3 million for each of the three month periods ended September 30, 2017 and September 30, 2016. Therapy engineering and product development costs decreased by \$0.1 million to \$1.0 million for the three months ended September 30, 2017 from \$1.1 million for the three months ended September 30, 2016. The Company continues to invest in strategic initiatives such as the development of clinical evidence in both Detection and Therapy, development of breast tomosynthesis products and ongoing enhancements to our electronic brachytherapy products.

*Marketing and Sales.* Marketing and sales expenses increased by \$0.3 million or 11.1%, from \$2.3 million in the three month period ended September 30, 2016 to \$2.6 million in the three month period ended September 30, 2017. Detection marketing and sales expense increased \$0.2 million from \$0.9 million in the three months ended September 30, 2016 to \$1.1 million for the three months ended September 30, 2017. The increase in Detection marketing and sales expenses was due primarily to increases in commissions and stock compensation. Therapy marketing and sales expense increased by \$0.1 million from \$1.5 million in the three months ended September 30, 2016 to \$1.6 million in the three months ended September 30, 2017.

*General and Administrative.* General and administrative expenses increased by \$0.2 million or 9.0%, from \$1.8 million in the three month period ended September 30, 2016 to \$1.9 million in the three month period ended September 30, 2017. The increase was due primarily to an increase in consulting and personnel costs.

**Table of Contents**

*Amortization and Depreciation.* Amortization and depreciation is primarily related to acquired intangible assets and depreciation related to machinery and equipment. Amortization and depreciation decreased to approximately \$0.1 million in the quarter ended September 30, 2017 from \$0.3 million for the quarter ended September 30, 2016. The decrease is due primarily to the sale of MRI assets in January 2017.

*Goodwill and long-lived asset impairment.* In the third quarter of 2017, the Company determined there was a triggering event, and accordingly completed an interim goodwill and long-lived asset impairment. In the quarter ended September 30, 2017, the Company recorded an impairment charge of \$4.0 million related to goodwill and \$0.7 million related to intangible assets.

**Other Income and Expense: (in thousands)**

	<b>Three months ended September 30,</b>			
	2017	2016	Change	Change %
Interest expense	\$ (36)	\$ (15)	(21)	140.0%
Interest income	3	2	1	50.0%
	\$ (33)	\$ (13)	\$ (20)	153.8%

Tax benefit (expense) \$ 42 \$ (10) \$ 52 (520.0)%

*Interest expense.* Interest expense of \$36,000 increased by \$21,000 or 140.0% for the three month period ended September 30, 2017 as compared to interest expense of \$15,000 in the three month period ended September 30, 2016. The increase in interest expense is due primarily to the interest expense associated with the Silicon Valley Bank term loan signed in August, 2017.

*Other income.* Other income was \$3,000 and \$2,000, respectively, for the three month periods ended September 30, 2017 and 2016.

*Tax benefit (expense).* The Company had a tax benefit of \$42,000 for the three month period ended September 30, 2017 as compared to tax expense of \$10,000 for the three month period ended September 30, 2016. The tax benefit for the quarter ended September 30, 2017 is the result of applying for New Hampshire research and development credits. Tax expense for the quarter ended September 30, 2016 is due primarily to state non-income and franchise based taxes.

**Nine months ended September 30, 2017 compared to the nine months ended September 30, 2016****Revenue: (in thousands)**

**Table of Contents**

	Nine months ended September 30,			
	2017	2016	Change	% Change
<b>Detection revenue</b>				
Product revenue	\$ 7,970	\$ 6,580	\$ 1,390	21.1%
Service revenue	5,096	6,381	(1,285)	(20.1)%
Subtotal	13,066	12,961	105	0.8%
<b>Therapy revenue</b>				
Product revenue	1,255	880	375	42.6%
Service revenue	5,879	5,569	310	5.6%
Subtotal	7,134	6,449	685	10.6%
<b>Total revenue</b>	<b>\$ 20,200</b>	<b>\$ 19,410</b>	<b>\$ 790</b>	<b>4.1%</b>

*Nine months ended September 30, 2017 and 2016:*

Total revenue for the nine month period ended September 30, 2017 was \$20.2 million compared with revenue of \$19.4 million for the nine month period ended September 30, 2016, an increase of approximately \$0.8 million, or 4.1%. The increase in revenue was due to a \$0.7 million increase in Therapy revenue and an increase in Detection revenues of approximately \$0.1 million.

Detection product revenue increased by approximately \$1.4 million from \$6.6 million to \$8.0 million or 21.1% in the nine months ended September 30, 2017 as compared to the nine months ended September 30, 2016. The increase is due primarily to an increase in CAD revenues of \$2.2 million offset by decreases in MRI revenue of approximately \$0.7 million and \$0.1 million in colon revenue. The decrease in MRI revenue is due primarily to the sale of the Company's MRI assets in January 2017.

Detection service and supplies revenue decreased by approximately \$1.3 million from \$6.4 million in the nine months ended September 30, 2016 to \$5.1 million in the nine months ended September 30, 2017. The decrease in service and supplies is due primarily to the sale of the Company's MRI assets in January 2017. Service and supplies revenue reflects the sale of service contracts to our installed base of customers. We expect service and supplies revenue related to our installed base of customers to vary from quarter to quarter as customers transition from 2D CAD to digital tomosynthesis.

Therapy product revenue was approximately \$1.3 million for the nine months ended September 30, 2017 as compared to \$0.9 million for the nine months ended September 30, 2016. Product revenue from the sale of our Axxent eBx systems can vary significantly due to an increase or decrease in the number of units sold which can cause a significant fluctuation in product revenue in the period.

Therapy service and supplies revenue increased approximately \$0.3 million from \$5.6 million in the nine months ended September 30, 2016 to \$5.9 million for the nine months ended September 30, 2017. The increase in Therapy service and supplies revenue is due primarily to an increase in the services related to electronic brachytherapy for NMSC.



**Table of Contents****Cost of Revenue and Gross Profit: (in thousands)**

	<b>Nine months ended September 30,</b>			
	<b>2017</b>	<b>2016</b>	<b>Change</b>	<b>% Change</b>
Products	\$ 1,349	\$ 611	\$ 738	120.8%
Service and supplies	4,169	3,911	258	6.6%
Amortization and depreciation	847	899	(52)	(5.8)%
Total cost of revenue	\$ 6,365	\$ 5,421	\$ 944	17.4%
Gross profit	\$ 13,835	\$ 13,989	\$ (154)	(1.1)%
Gross profit %	68.5%	72.1%		(3.6)%

  

	<b>Nine months ended September 30,</b>			
	<b>2017</b>	<b>2016</b>	<b>Change</b>	<b>% Change</b>
Detection gross profit	\$ 11,553	\$ 11,429	\$ 124	1.1%
Therapy gross profit	2,282	2,560	(278)	(10.9)%
Gross profit	\$ 13,835	\$ 13,989	\$ (154)	(1.1)%

Gross profit for the nine month period ended September 30, 2017 was \$13.9 million, or 68.5% of revenue as compared to \$14.0 million or 72.1% of revenue in the nine month period ended September 30, 2016. Gross profit percent changes are primarily due to changes in the mix of business, consulting costs related to non-recurring engineering revenue, additional manufacturing investments and amortization of acquired intangibles. Gross profit for the nine months ended September 30, 2016 includes a recovery of the medical device excise tax of approximately \$0.5 million due to a refund.

Cost of products increased by approximately \$0.7 million to \$1.3 million for the nine months ended September 30, 2017 from approximately \$0.6 million for the nine months ended September 30, 2016, which is due primarily to an increase in Detection product revenue as well as a recovery of medical device excise tax in cost of product revenue of \$0.3 million in 2016. The cost of product revenue as a percentage of product revenue was approximately 15% for the nine months ended September 30, 2017 as compared to 8% for the nine months ended September 30, 2016. The increase in cost of product revenue as a percentage of product revenue is due primarily to the recovery of medical device excise tax in 2016. Cost of product revenue can vary due to product mix.

The cost of service and supplies increased by \$0.3 million from \$3.9 million in the nine months ended September 30, 2016 to \$4.2 million in the nine months ended September 30, 2017. The cost of service and supplies revenue as a percentage of service and supplies revenue was approximately 38% for the quarter ended September 30, 2017 and 33% for the quarter ended September 30, 2016. The increase in cost of service supplies is due primarily to the recovery of medical device excise tax of \$0.2 million in 2016, which also decreased the cost of service and supplies revenue as a percentage of revenue in 2016.





**Table of Contents**

Amortization and depreciation was approximately \$0.9 million in each of the nine months ended September 30, 2016 and September 30, 2017.

**Operating Expenses: (in thousands)**

	<b>Nine months ended September 30,</b>			
	2017	2016	Change	Change %
<b>Operating expenses:</b>				
Engineering and product development	\$ 7,060	\$ 6,835	\$ 225	3.3%
Marketing and sales	8,172	7,379	793	10.7%
General and administrative	6,067	5,586	481	8.6%
Amortization and depreciation	345	867	(522)	(60.2)%
Goodwill and long-lived asset impairment	4,700		4,700	0.0%
Gain from sale of MRI assets	(2,508)		(2,508)	0.0%
 Total operating expenses	 \$ 23,836	 \$ 20,667	 \$ 3,169	 15.3%

Operating expenses increased by approximately \$3.2 million or 15.3% in the nine months ended September 30, 2017 as compared to the nine months ended September 30, 2016. In the first quarter of 2017, the Company sold certain MRI assets to Invivo and recorded a gain on the sale of \$2.5 million, which was offset by the goodwill and long lived asset impairment of \$4.7 million, recorded in the third quarter of 2017.

*Engineering and Product Development.* Engineering and product development costs were approximately \$7.1 million for the nine month period ended September 30, 2017 as compared to \$6.8 million for the nine month period ended September 30, 2016, an increase of \$225,000 or 3.3%. Therapy engineering and product development costs increased from \$3.1 million in the nine months ended September 30, 2016 to \$3.2 million for the nine months ended September 30, 2017. Detection engineering and product development costs increased by \$0.2 million to \$3.9 million for the nine month period ended September 30, 2017 from \$3.7 million for the nine month period ended September 30, 2016. The Company continues to invest in strategic initiatives such as the development of ongoing clinical evidence, development of breast tomosynthesis products and additional enhancements to our electronic brachytherapy products.

*Marketing and Sales.* Marketing and sales expenses increased by \$0.8 million or 10.7%, from \$7.4 million in the nine month period ended September 30, 2016 to \$8.2 million in the nine month period ended September 30, 2017. Therapy marketing and sales expense increased \$0.2 million from \$4.7 million in the nine months ended September 30, 2016 to \$4.9 million for the nine months ended September 30, 2017. Detection marketing and sales costs increased by \$0.5 million from \$2.7 million in the nine months ended September 30, 2016 to \$3.2 million for the nine months ended September 30, 2017. The increase in Detection marketing and sales costs is due primarily to increases in commissions and stock compensation.

*General and Administrative.* General and administrative expenses increased by \$0.5 million from \$5.6 million in the nine month period ended September 30, 2016 to \$6.1 million in the nine month period ended September 30, 2017. The increase was due primarily to an increase in stock compensation costs and a \$249,000 gain on settlement of litigation related to the acquisition of VuComp M-Vu CAD in January 2016.



**Table of Contents**

*Amortization and Depreciation.* Amortization and depreciation is primarily related to acquired intangible assets and depreciation related to machinery and equipment. Amortization and depreciation decreased by \$0.5 million from \$0.9 million in the nine month period ended September 30, 2016 to \$0.3 million in the nine month period ended September 30, 2017. The decrease is due primarily to the sale of MRI assets in January 2017.

*Gain from sale of MRI assets.* The Company entered into an Asset Purchase Agreement with Invivo Corporation to sell certain MRI assets in December 2016 and the transaction closed on January 30, 2017. As a result, the Company recorded a gain on sale from MRI assets of \$2.5 million in the first quarter of 2016.

*Goodwill and long-lived asset impairment.* In the third quarter of 2017, the Company determined there was a triggering event, and accordingly completed an interim goodwill and long-lived asset impairment. In the quarter ended September 30, 2017, the Company recorded an impairment charge of \$4.0 million related to goodwill and \$0.7 million related to intangible assets.

**Other Income and Expense: (in thousands)**

	<b>Nine months ended September 30,</b>			
	2017	2016	Change	Change %
Interest expense	\$ (51)	\$ (59)	\$ 8	(13.6)%
Interest income	3	9	(6)	(66.7)%
	\$ (48)	\$ (50)	\$ 2	(4.0)%
Tax benefit (expense)	\$ 28	\$ (55)	\$ 83	(150.9)%

*Interest expense.* Interest expense of \$51,000 decreased by \$8,000 or 13.6% for the nine month period ended September 30, 2017 as compared to interest expense of \$59,000 in the nine month period ended September 30, 2016. Interest expense for the nine months ended September 30, 2017 relates primarily to notes payable. Interest expense in for the nine months ended September 30, 2016 related primarily to capital leases which were paid in 2017.

*Interest income.* Interest income was \$3,000 and \$9,000 for the nine month period ended September 30, 2017 and September 30, 2016, respectively which reflected income earned from our money market accounts.

*Tax benefit (expense).* The Company had a tax benefit of \$28,000 for the nine month period ended September 30, 2017 as compared to tax expense of \$55,000 for the nine month period ended September 30, 2016. The tax benefit for the nine months ended September 30, 2017 is the result of applying for New Hampshire research and development credits. Tax expense for the nine months ended September 30, 2016 is due primarily to state non-income and franchise based taxes.

**Liquidity and Capital Resources**

**Table of Contents**

We believe that our current liquidity and capital resources are sufficient to sustain operations through at least the next 12 months, primarily due to cash on hand. Our projected cash needs include planned capital expenditures, lease and settlement commitments, and other long-term obligations.

As of September 30, 2017, the Company has current assets of \$22.4 million which includes \$11.3 million of cash and cash equivalents. Current liabilities are \$11.6 million and working capital is \$10.8 million. The ratio of current assets to current liabilities was 1.92:1. In January 2017, the Company received \$2.8 million from the sale of MRI assets to Invivo. In August 2017 the Company entered into a debt facility that provides an initial term loan of \$6.0 million and a \$4.0 million revolving line of credit. The Company also has the option to secure an additional \$3.0 million in term loan in 2018, subject to meeting certain revenue milestones.

	<b>For the nine months ended September 30,</b>	
	<b>2017</b>	<b>2016</b>
	(in thousands)	
Net cash used for operating activities	\$ (5,565)	\$ (3,862)
Net cash provided by (used for) investing activities	2,486	(262)
Net cash provided by (used for) financing activities	5,755	(673)
Increase (decrease) in cash and equivalents	\$ 2,676	\$ (4,797)

Net cash used for operating activities for the nine month period ended September 30, 2017 was \$5.6 million, compared to net cash used for operating activities of \$3.9 million for the nine month period ended September 30, 2016. The cash used for operating activities for the nine month period ended September 30, 2017 resulted primarily from our net loss and from working capital changes resulting from increases in accounts receivable, decreases in accounts payable and accrued expenses offset by the cash provided due to the decrease in prepaid expenses. We expect that cash used for or provided by operating activities may fluctuate in future periods as a result of a number of factors, including fluctuations in our operating results, specifically the timing of when we recognize revenue, our accounts receivable collections and the timing of other payments.

The net cash provided by investing activities for the nine month period ended September 30, 2017 of \$2.5 million was due to the cash received from the sale of MRI assets offset by purchases of property and equipment. Cash used for investing activities for the nine month period ended September 30, 2016 was \$0.3 million, which represents primarily purchases of property and equipment.

Net cash provided by financing activities for the nine month period ended September 30, 2017 was \$5.8 million as compared to net cash used for financing activities of \$0.7 million for the nine month period ended September 30, 2016. Cash provided by financing activities for the nine months ended September 30, 2017 is due primarily to proceeds from the \$6.0 million term loan and taxes paid on the issuance of restricted stock to employees. Cash used for financing activities for the nine month period ended September 30, 2016 represents primarily repayments of capital leases.

**Table of Contents****Contractual Obligations**

The following table summarizes, for the periods presented, our future estimated cash payments under existing contractual obligations (in thousands).

<b>Contractual Obligations</b>	<b>Total</b>	<b>Payments due by period</b>			
		<b>Less than 1 year</b>	<b>1-3 years</b>	<b>3-5 years</b>	<b>5+ years</b>
Operating Lease Obligations	\$ 1,848	\$ 742	\$ 1,106	\$	\$
Capital lease obligations	42	\$ 12	30		
Settlement Obligations	500	500			
Notes Payable	6,615	591	4,324	1,700	
Other Commitments	825	632	84	32	77
<b>Total Contractual Obligations</b>	<b>\$ 9,830</b>	<b>\$ 2,477</b>	<b>\$ 5,544</b>	<b>\$ 1,732</b>	<b>\$ 77</b>

Operating lease obligations are the minimum payments due under these obligations.

Settlement obligations represent the remaining payments of the obligations to Hologic. The Company paid \$0.5 million in July 2017 which represented the remaining settlement obligation to Zeiss.

Other commitments represent firm purchase obligations to suppliers for future product and service deliverables.

**Recent Accounting Pronouncements**

See Note 14 to the Condensed Consolidated Financial Statements.

**Table of Contents**

**Item 3. Quantitative and Qualitative Disclosures about Market Risk**

We believe we are not subject to material foreign currency exchange rate fluctuations, as substantially all of our sales and expenses are denominated in the U.S. dollar. We do not hold derivative securities and have not entered into contracts embedded with derivative instruments, such as foreign currency and interest rate swaps, options, forwards, futures, collars or warrants, either to hedge existing risks or for speculative purposes.

**Item 4. Controls and Procedures**

Our management, with the participation of our principal executive officer and principal financial officer, evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this report. Based on this evaluation, as of September 30, 2017, the principal executive officer and principal financial officer concluded that our disclosure controls and procedures (as defined in Rule 13a-15(e) of the Securities Exchange Act of 1934 ( Exchange Act )) were effective at the reasonable level of assurance.

A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected. We conduct periodic evaluations to enhance, where necessary our procedures and controls.

Our principal executive officer and principal financial officer conducted an evaluation of our internal control over financial reporting (as defined in Exchange Act Rule 13a-15(f)) to determine whether any changes in internal control over financial reporting occurred during the quarter ended September 30, 2017, that have materially affected or which are reasonably likely to materially affect internal control over financial reporting. Based on that evaluation, there has been no such change during such period.

**Table of Contents****PART II OTHER INFORMATION****Item 1. Legal Proceedings**

Please refer to the detailed discussion regarding litigation set forth in Note 8 of the Notes to Condensed Consolidated Financial Statements in this Form 10-Q.

The Company is involved in various legal matters that are in the process of litigation or settled in the ordinary course of business. Although the final results of all such matters and claims cannot be predicted with certainty, we believe that the ultimate resolution of all such matters and claims will not have a material adverse effect on our financial condition. However, such matters could have a material adverse effect on our operating results and cash flows for a particular period.

**Item 1A. Risk Factors:**

We operate in a changing environment that involves numerous known and unknown risks and uncertainties that could materially adversely affect our operations. Our risk factors are described in Part I, Item 1A of our Annual Report on Form 10-K filed with the SEC for the year ended December 31, 2016 as filed with the SEC on March 24, 2017. There have been no material changes in the risks affecting iCAD since the filing of our Form 10-K.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

Month of purchase	Total number of shares purchased (1)	Average price paid per share	Maximum dollar	
			Total number of shares purchased as part of publicly announced plans or programs	value of shares that may yet be purchased under the plans or programs
July 1 - July 31, 2017		\$	\$	\$
August 1 - August 30, 2017	7,629	3.77		
September 1 - September 31, 2017				
Total	7,629	\$ 3.77	\$	\$

- (1) Represents shares of common stock surrendered by employees to the Company to pay employee withholding taxes due upon the vesting of restricted stock.

**Item 6. Exhibits**

Exhibit No.	Description
31.1	<u>Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*</u>
31.2	<u>Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*</u>



**Table of Contents**

- 32.1 Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. \*
- 32.2 Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. \*
- 101 The following materials formatted in XBRL (eXtensible Business Reporting Language); (i) Consolidated Balance Sheets as of September 30, 2017 and December 31, 2016, (ii) Consolidated Statements of Operations for the three and nine months ended September 30, 2017 and 2016, (iii) Consolidated Statements of Cash Flows for the nine months ended September 30, 2017 and 2016, and (iv) Notes to Consolidated Financial Statements.

**Table of Contents**

Signatures

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

iCAD, Inc.  
(Registrant)

Date: November 14, 2017

By: /s/ Kenneth M. Ferry  
Kenneth M. Ferry  
Chief Executive Officer,

Director

Date: November 14, 2017

By: /s/ Richard Christopher  
Richard Christopher

Chief Financial Officer