

INSIGNIA SYSTEMS INC/MN
Form 10-Q
November 14, 2018

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

FORM 10-Q

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

for the quarterly period ended September 30, 2018
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: 1-13471

INSIGNIA SYSTEMS, INC.
(Exact name of registrant as specified in its charter)

Minnesota 41-1656308
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

8799 Brooklyn Blvd., Minneapolis, MN 55445
(Address of principal executive offices; zip code)

(763) 392-6200
(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer

Accelerated filer

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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

Number of shares outstanding of Common Stock, \$.01 par value, as of November 9, 2018 was 11,839,774.

Insignia Systems, Inc.

TABLE OF CONTENTS

	Page
PART I. FINANCIAL INFORMATION	
Item 1. Financial Statements	
<u>Condensed Balance Sheets – September 30, 2018 (unaudited) and December 31, 2017</u>	1
<u>Condensed Statements of Operations – Three and nine months ended September 30, 2018 and 2017 (unaudited)</u>	2
<u>Condensed Statements of Cash Flows – Nine months ended September 30, 2018 and 2017 (unaudited)</u>	
<u>Notes to Financial Statements – September 30, 2018 (unaudited)</u>	4
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	10
Item 3. <u>Quantitative and Qualitative Disclosures about Market Risk</u>	15
Item 4. <u>Controls and Procedures</u>	15
PART II. <u>OTHER INFORMATION</u>	
Item 1. <u>Legal Proceedings</u>	15
Item 1A. <u>Risk Factors</u>	15
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	16
Item 3. <u>Defaults upon Senior Securities</u>	16
Item 4. <u>Mine Safety Disclosures</u>	16
Item 5. <u>Other Information</u>	16
Item 6. <u>Exhibits</u>	17

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Insignia Systems, Inc.

CONDENSED BALANCE SHEETS

	September 30,	
	2018	December 31,
	(Unaudited)	2017
ASSETS		
Current Assets:		
Cash and cash equivalents	\$7,590,000	\$4,695,000
Accounts receivable, net	11,294,000	11,864,000
Inventories	323,000	301,000
Income tax receivable	94,000	360,000
Prepaid expenses and other	335,000	415,000
Total Current Assets	19,636,000	17,635,000
Other Assets:		
Property and equipment, net	3,049,000	2,670,000
Other, net	1,078,000	1,383,000
Total Assets	\$23,763,000	\$21,688,000
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	3,739,000	3,232,000
Accrued liabilities:		
Compensation	1,503,000	1,531,000
Other	938,000	667,000
Deferred revenue	753,000	372,000
Total Current Liabilities	\$6,933,000	\$5,802,000

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Long-Term Liabilities:		
Deferred tax liabilities	236,000	245,000
Accrued income taxes	604,000	581,000
Deferred rent	173,000	219,000
Total Long-Term Liabilities	\$1,013,000	\$1,045,000
Commitments and Contingencies	—	—
Shareholders' Equity:		
Common stock, par value \$.01:		
Authorized shares - 40,000,000		
Issued and outstanding shares - 11,848,000 at September 30, 2018 and 11,914,000 at December 31, 2017	118,000	119,000
Additional paid-in capital	15,345,000	15,361,000
Retained earnings (Accumulated deficit)	354,000	(639,000)
Total Shareholders' Equity	15,817,000	14,841,000
Total Liabilities and Shareholders' Equity	\$23,763,000	\$21,688,000

See accompanying notes to financial statements.

Table of Contents

Insignia Systems, Inc.

CONDENSED
STATEMENTS OF
OPERATIONS

(Unaudited)

Three	Nine
Months	Months
Ended	Ended

September 30	September
	30

	2018	2017	2018	2017
Services revenues	\$9,069,000	\$7,353,000	\$23,963,000	\$17,169,000
Products revenues	386,000	370,000	1,156,000	1,170,000
Total Net Sales	9,455,000	7,723,000	25,119,000	18,339,000
Cost of services	5,569,000	4,700,000	14,937,000	12,624,000
Cost of goods sold	323,000	280,000	868,000	845,000
Total Cost of Sales	5,892,000	4,980,000	15,805,000	13,469,000
Gross Profit	3,563,000	2,743,000	9,314,000	4,870,000
Operating Expenses:				
Selling	908,000	879,000	2,530,000	2,598,000
Marketing	703,000	409,000	1,873,000	1,262,000
General and administrative	1,106,000	1,004,000	3,580,000	2,871,000
Total Operating Expenses	2,717,000	2,292,000	7,983,000	6,731,000
Operating Income (Loss)	846,000	451,000	1,331,000	(1,861,000)
Other income	15,000	2,000	27,000	7,000
Income (Loss) Before Taxes	861,000	453,000	1,358,000	(1,854,000)
Income tax expense (benefit)	216,000	2,000	365,000	(580,000)
Net Income (Loss)	\$645,000	\$451,000	\$993,000	\$(1,274,000)
Net income (loss) per share:				
Basic	\$0.05	\$0.04	\$0.08	\$(0.10)
Diluted	\$0.05	\$0.04	\$0.08	\$(0.10)

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Shares used in calculation of net income (loss) per share:

Basic	11,729,000	11,758,000	11,784,000	11,698,000
Diluted	12,012,000	11,777,000	12,026,000	11,698,000

See accompanying notes to financial statements.

Table of Contents

Insignia Systems, Inc.

CONDENSED STATEMENTS OF CASH FLOWS

(Unaudited)

Nine Months Ended September 30	2018	2017
Operating Activities:		
Net income (loss)	\$993,000	\$(1,274,000)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	860,000	1,001,000
Changes in allowance for doubtful accounts	(16,000)	16,000
Deferred income tax expense	(9,000)	(205,000)
Stock-based compensation expense	277,000	317,000
Changes in operating assets and liabilities:		
Accounts receivable	586,000	(2,040,000)
Inventories	(22,000)	(1,000)
Income tax receivable	266,000	355,000
Prepaid expenses and other	80,000	192,000
Accounts payable	408,000	777,000
Accrued liabilities	253,000	377,000
Income tax payable	—	20,000
Accrued income taxes	23,000	—
Deferred revenue	381,000	586,000
Net cash provided by operating activities	4,080,000	121,000
Investing Activities:		
Purchases of property and equipment	(877,000)	(822,000)
Net cash used in investing activities	(877,000)	(822,000)
Financing Activities:		
Cash dividends paid (\$0.70 per share)	(14,000)	(8,177,000)
Proceeds from issuance of common stock, net	49,000	(14,000)
Repurchase of common stock upon vesting of restricted stock awards	(74,000)	—
Repurchase of common stock, net	(269,000)	—
Net cash used in financing activities	(308,000)	(8,191,000)
Increase (decrease) in cash and cash equivalents	2,895,000	(8,892,000)

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Cash and cash equivalents at beginning of period	4,695,000	12,267,000
Cash and cash equivalents at end of period	\$7,590,000	\$3,375,000

Supplemental disclosures for cash flow information:

Cash paid during the period for income taxes	\$84,000	\$2,000
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Non-cash investing and financing activities:

Purchases of property and equipment included in accounts payable	\$96,000	\$115,000
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See accompanying notes to financial statements.

Table of Contents

Insignia Systems, Inc.
Notes To Financial Statements
(Unaudited)

1. Summary of Significant Accounting Policies.

Description of Business. Insignia Systems, Inc. (the “Company”) markets in-store advertising products, programs and services to retailers and consumer packaged goods manufacturers. The Company operates in a single reportable segment. The Company’s primary products include the Insignia Point-of-Purchase Services (POPS®), freshADSsm and other retailer approved promotional services, in-store marketing programs, and custom adhesive and non-adhesive signage materials directly to our retail customers.

Basis of Presentation. The accompanying unaudited financial statements of the Company have been prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) for interim financial information. They do not include all information and footnotes required by U.S. GAAP for complete financial statements. However, except as described herein, there has been no material change in the information disclosed in the notes to financial statements included in our financial statements as of and for the year ended December 31, 2017 included in the Company’s Annual Report on Form 10-K. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Results of operations for the periods presented are not necessarily indicative of the results to be expected for the full year.

Recently Adopted Accounting Pronouncements. Effective January 1, 2018, the Company adopted Financial Accounting Standards Board Accounting Standards Update (“ASU”) 2014-09 “Revenue from Contracts with Customers” (“Topic 606”). Topic 606 supersedes the revenue recognition requirements in Topic 605 “Revenue Recognition,” and requires entities to recognize revenue when control of the promised goods or services is transferred to customers at an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services. The adoption of ASU 2014-09, using the modified retrospective approach, had no significant impact on our results of operations, cash flows, or financial position. Revenue continues to be recognized for POPSigns ratably over the period of service, which is typically a two-week display cycle, and for sign card sales, at the time the products are shipped to customers. Additional information and disclosures required by this new standard are contained in Note 2, “Revenue.”

Inventories. Inventories are primarily comprised of sign cards, hardware and roll stock. Inventory is valued at the lower of cost or net realizable value using the first-in, first-out (FIFO) method, and consisted of the following as of the dates indicated:

	September 30,	December 31,
	2018	2017
Raw materials	\$90,000	\$68,000
Work-in-process	3,000	10,000
Finished goods	230,000	223,000
	\$323,000	\$301,000

Table of Contents

Property and Equipment. Property and equipment consisted of the following as of the dates indicated:

	September 30,	December 31,
	2018	2017
Property and Equipment:		
Production tooling, machinery and equipment	\$4,087,000	\$4,003,000
Office furniture and fixtures	329,000	325,000
Computer equipment and software	2,726,000	2,680,000
Leasehold improvements	577,000	577,000
Construction in-progress	995,000	206,000
	8,714,000	7,791,000
Accumulated depreciation and amortization	(5,665,000)	(5,121,000)
Net Property and Equipment	\$3,049,000	\$2,670,000

Depreciation expense was approximately \$188,000 and \$555,000 in the three and nine months ended September 30, 2018, respectively, and \$220,000 and \$653,000 in the three and nine months ended September 30, 2017, respectively.

Stock-Based Compensation. We measure and recognize compensation expense for all stock-based payments at fair value. Restricted stock units and awards are valued at the closing market price of the Company's stock on the date of the grant. We use the Black-Scholes option pricing model to determine the weighted average fair value of options and employee stock purchase plan rights. The determination of fair value of share-based payment awards on the date of grant using an option-pricing model is affected by our stock price as well as by assumptions regarding a number of complex and subjective variables. These variables include, but are not limited to, the expected stock price volatility over the term of the awards, and actual and projected employee stock option exercise behaviors.

On November 28, 2016, our Board of Directors amended the 2003 Incentive Stock Option Plan (the "2003 Plan") and the 2013 Omnibus Stock and Incentive Plan (the "2013 Plan") to permit equitable adjustments to outstanding awards in the event of an extraordinary cash dividend. On March 28, 2017, the Board of Directors approved the modification of all outstanding stock option awards to provide option holders with substantially equivalent economic value after the effect of the dividend. The modification resulted in the issuance of options to purchase 150,476 additional shares. Total stock-based compensation expense for the modifications was approximately \$79,000, which was recorded during the nine months ended September 30, 2017.

During the nine months ended September 30, 2018, stock option awards to purchase up to 119,515 shares were granted by the Company. The Company estimates the fair value of these awards using the following weighted average assumptions: expected life of 6.5 years, expected volatility of 51.21%, dividend yield of 0% and a risk-free rate interest rate of 2.80%. During the nine months ended September 30, 2017, no other stock option awards were granted by the Company beyond the modification discussed above.

During the nine months ended September 30, 2018, the Company issued 297,515 restricted stock units under the 2013 Plan and the 2018 Equity Incentive Plan (the "2018 Plan"). The shares underlying the awards were assigned a value of

\$1.77 and \$1.95 per share, which was the closing price of our common stock on the date of grants. These awards are scheduled to vest over three years or four years with the first vesting in year two. During the nine months ended September 30, 2017, the Company issued 143,424 restricted stock units under the 2013 Plan. The shares underlying the awards made in 2017 were assigned weighted average values of \$1.13 per share based on the closing price of our common stock on the applicable dates of grant and are scheduled to vest over two years.

During the nine months ended September 30, 2018, no restricted stock was issued. During the nine months ended September 30, 2017, the Company issued 60,000 shares of restricted stock under the 2013 Plan. The shares underlying the awards were assigned a value of \$1.09 per share, which was the closing price of our common stock on the date of grant and are scheduled to vest over the two years following the date of grant.

Table of Contents

During July 2018, non-employee members of the Board of Directors received restricted stock grants totaling 46,152 shares pursuant to the 2018 Plan. The shares underlying the awards were assigned a value of \$1.95 per share, which was the closing price of our common stock on the date of grants, for a total value of \$90,000, and are scheduled to vest the day immediately preceding the date of the next annual shareholder meeting. During June 2017, non-employee members of the Board of Directors received grants totaling 72,115 fully vested shares of common stock pursuant to the 2013 Plan. The shares were assigned a value of \$1.04 per share, based on the closing price on the grant date, for a total value of \$75,000, which is included in stock-based compensation expense for the nine months ended September 30, 2017.

Total stock-based compensation expense recorded for the three and nine months ended September 30, 2018 was \$128,000 and \$277,000, respectively, and for the three and nine months ended September 30, 2017 was \$43,000 and \$317,000, respectively.

During the three and nine months ended September 30, 2018, there were approximately 900 shares issued pursuant to stock option exercises, for which the Company received proceeds of \$1,000. During the three and nine months ended September 30, 2017, there were no options exercised. A portion of the stock option exercises in the three and nine months ended September 30, 2018 were completed on a cashless basis.

The Company estimated the fair value of stock-based awards granted during the nine months ended September 30, 2018, under the Company's employee stock purchase plan using the following weighted average assumptions: expected life of 1.0 years, expected volatility of 66%, dividend yield of 0% and risk-free interest rate of 1.83%.

Net Income (Loss) per Share. Basic net income (loss) per share is computed by dividing net income (loss) by the weighted average shares outstanding and excludes any potential dilutive effects of stock options and restricted stock units and awards. Diluted net income (loss) per share gives effect to all diluted potential common shares outstanding during the period.

Options to purchase approximately 305,000 and 265,000 shares of common stock with a weighted average exercise price of \$2.66 and \$3.22, respectively, were outstanding at September 30, 2018 and were not included in the computation of common stock equivalents for the three and nine months ended September 30, 2018 because their exercise prices were higher than the average fair market value of the common stock during the reporting period.

Options to purchase approximately 501,000 shares of common stock with a weighted average exercise price of \$2.33 were outstanding at September 30, 2017 and were not included in the computation of common stock equivalents for the three months ended September 30, 2017 because their exercise prices were higher than the average fair market value of the common shares during the reporting period. Due to the net loss incurred during the nine months ended September 30, 2017 all stock options were anti-dilutive for that period.

Weighted average common shares outstanding for the three and nine months ended September 30, 2018 and 2017 were as follows:

Three Months Ended	Nine Months Ended
September 30	September 30

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	2018	2017	2018	2017
Denominator for basic net income (loss) per share - weighted average shares	11,729,000	11,758,000	11,784,000	11,698,000
Effect of dilutive securities:				
Stock options and restricted stock units and awards	283,000	19,000	242,000	—
Denominator for diluted net income (loss) per share - weighted average shares	12,012,000	11,777,000	12,026,000	11,698,000

Dividends. On November 28, 2016, the Board declared a one-time special dividend of \$0.70 per share to shareholders of record as of December 16, 2016 of \$8,233,000, of which \$8,163,000 was paid on January 6, 2017, \$14,000 was paid on May 15, 2017, and an additional \$14,000 was paid on May 15, 2018.

Table of Contents

2. Revenue Recognition. Under Topic 606, revenue is measured based on consideration specified in the contract with a customer, adjusted for any applicable estimates of variable consideration and other factors affecting the transaction price, including noncash consideration, consideration paid or payable to a customer and significant financing components. Revenue from all customers is recognized when a performance obligation is satisfied by transferring control of a distinct good or service to a customer, as further described below under “Performance Obligations.”

Taxes collected from customers and remitted to governmental authorities are excluded from revenue on the net basis of accounting.

The Company includes shipping and handling fees in revenues. Shipping and handling costs associated with outbound freight after control over a product has transferred to a customer are accounted for as a fulfillment cost and are included in cost of goods sold.

The majority of the Company’s accounts receivable is due from companies in the consumer-packaged goods industry. Credit is extended based on evaluation of a customer’s financial condition and, generally, collateral is not required. Accounts receivable are due within 30-150 days and are stated at amounts due from customers, net of an allowance for doubtful accounts.

Performance Obligations

A performance obligation is a promise in a contract to transfer a distinct good or service to the customer and is the unit of account under Topic 606. A contract’s transaction price is allocated to each distinct performance obligation and recognized as revenue when, or as, the performance obligation is satisfied. The following is a description of our performance obligations included in our primary revenue streams and the timing or method of revenue recognition for each:

POPSign Services. Our primary source of revenue is from marketing in-store advertising programs and services primarily to consumer-packaged goods (“CPG”) manufacturers. We provide a service of displaying promotional signs in close proximity to the manufacturer’s product in participating stores, which we maintain in two-to-four-week cycle increments. Our in-store marketing programs include POPSigns and freshADS (together referred to herein as “POPSign services”).

Each of the individual activities under our POPSign services, including production activities, are inputs to an integrated sign display service. As such, each POPSign service represents a single performance obligation. Customers receive and consume the benefits from the promotional displays over the duration of the contracted display cycle. Additionally, the display of the signs does not have an alternative use to us and we have an enforceable right to payment for services performed to date. As a result, we recognize the transaction price for our POPSign service performance obligations as revenue over time. Given the nature of our performance obligations is to provide a display service over the duration of a specified period or periods, we recognize revenue on a straight-line basis over the display service period as it best reflects the timing of transfer of our POPSign services.

Other Service Revenues. The Company also supplies CPG manufactures with other miscellaneous retailer approved promotional services and sign solutions. These services are more customized than the POPSign program, consisting of variable durations and variable specifications. Due to the variable nature of these services, revenue recognition is a mix of over time and point in time recognition.

Products. We also sell custom adhesive and non-adhesive signage materials directly to our customers. Each such product is a distinct performance obligation. Revenue is recognized at a point in time upon shipment, when control of the goods transfers to the customer.

Table of Contents

Disaggregation of Revenue

In the following table, revenue is disaggregated by major revenue stream and timing of revenue recognition.

	Three months ended September 30, 2018			Nine months ended September 30, 2018		
	Services Revenues	Products Revenue	Total Revenue	Services Revenues	Products Revenue	Total Revenue
Timing of revenue recognition:						
Products and services transferred over time		\$8,016,000				