CUTERA INC
Form 10-Q
November 08, 2006
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2006

OR

¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period ______ to ______ .

Commission file number: 000-50644

CUTERA, INC.

(Exact name of registrant as specified in its charter)

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

3240 Bayshore Blvd., Brisbane, California 94005

(Address of principal executive offices)

(415) 657-5500

(Registrant s telephone number, including area code)

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act (check one):

Large accelerated filer ¨ Accelerated filer x Non-accelerated filer ¨

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

The number of shares of Registrant s common stock issued and outstanding as of October 31, 2006 was 12,755,798.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

CUTERA, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands)

(unaudited)

	September 30, 2006	December 31, 2005
Assets		
Current assets:		
Cash and cash equivalents	$ 3,058	$ 5,260
Marketable investments	87,614	86,736
Accounts receivable, net	9,124	6,478
Inventory	5,558	5,245
Deferred tax asset	6,711	3,027
Other current assets	3,998	3,728
Total current assets	116,063	110,474
Property and equipment, net	992	1,015
Intangibles, net	1,515	469
Total assets	$ 118,570	$ 111,958
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	$ 1,396	$ 1,352
Accrued liabilities	12,657	9,131
Deferred revenue	3,126	1,673
Total current liabilities	17,179	12,156
Deferred rent	1,342	1,096
Deferred revenue, net of current portion	2,242	1,469
Deferred tax liability	60	60
Total liabilities	20,823	14,781
Stockholders equity:		
Common stock	13	12
Additional paid-in capital	81,510	77,705
Deferred stock-based compensation	(482)	(2,171)
Retained earnings	16,751	21,743
Accumulated other comprehensive loss	(45)	(112)
Total stockholders equity	97,747	97,177
Total liabilities and stockholders equity	$ 118,570	$ 111,958

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

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CUTERA, INC

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share data)

(unaudited)

	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005
Net revenue	$ 25,059	$ 18,950	$ 70,211	$ 51,667
Cost of revenue	7,931	4,746	21,510	13,642
Gross profit	17,128	14,204	48,701	38,025
Operating expenses:				
Sales and marketing	8,174	6,222	25,025	17,854
Research and development	1,679	1,334	4,538	3,932
General and administrative	2,992	1,924	11,615	6,519
Litigation settlement	544		18,935	
Total operating expenses	13,389	9,480	60,113	28,305
Income (loss) from operations	3,739	4,724	(11,412)	9,720
Interest and other income, net	829	549	2,615	1,351
Income (loss) before income taxes	4,568	5,273	(8,797)	11,071
Provision (benefit) for income taxes	1,618	1,472	(3,805)	3,080
Net income (loss)	$ 2,950	$ 3,801	$ (4,992)	$ 7,991
Net income (loss) per share:				
Basic	$ 0.23	$ 0.33	$ (0.40)	$ 0.70
Diluted	$ 0.21	$ 0.27	$ (0.40)	$ 0.58
Weighted-average number of shares used in per share calculations:				
Basic	12,675	11,661	12,460	11,369
Diluted	14,238	13,924	12,460	13,681

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

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CUTERA, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(unaudited)

	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005
Cash flows from operating activities:		
Net income (loss)	$ (4,992)	$ 7,991
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	636	503
Change in allowance for doubtful accounts	(63)	(296)
Provision for excess and obsolete inventory	90	434
Change in deferred taxes	(3,684)	612
Stock-based compensation	3,231	1,202
Tax benefit from stock option exercises		3,125
Changes in assets and liabilities:		
Accounts receivable	(2,583)	1,608
Inventory	(403)	(2,430)
Other current assets	(270)	(1,635)
Accounts payable	44	430
Accrued liabilities	3,414	359
Deferred rent	246	336
Deferred revenue	2,226	579
Net cash provided by (used in) operating activities	(2,108)	12,818
Cash flows from investing activities:		
Acquisition of property and equipment	(441)	(414)
Acquisition of intangibles	(1,218)	(165)
Proceeds from sales of marketable investments	12,303	18,294
Proceeds from maturities of marketable investments	76,693	34,373
Purchase of marketable investments	(89,807)	(70,995)
Net cash used in investing activities	(2,470)	(18,907)
Cash flows from financing activities:		
Proceeds from exercise of stock options and employee stock purchase plan	2,376	3,747
Net cash provided by financing activities	2,376	3,747
Net decrease in cash and cash equivalents	(2,202)	(2,342)
Cash and cash equivalents at beginning of period	5,260	7,070
Cash and cash equivalents at end of period	$ 3,058	$ 4,728
Supplemental and non-cash disclosure of cash flow information:		
Change in deferred stock-based compensation, net of terminations	$ (1,261)	$ 1,393

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

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Basis of Presentation

The condensed consolidated financial statements include the accounts of Cutera, Inc. (the Company), a Delaware corporation, and its wholly owned subsidiaries. All intercompany accounts and transactions have been eliminated.

The financial information furnished is unaudited. The condensed consolidated financial statements included in this report reflect all adjustments (consisting only of normal recurring adjustments) that the Company considers necessary for the fair statement of the results of operations for the interim periods covered and of the financial condition of the Company at the date of the interim balance sheet. The December 31, 2005 condensed consolidated balance sheet was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America. The results for interim periods are not necessarily indicative of the results for the entire year or any other interim period. The condensed consolidated financial statements should be read in conjunction with the Company s financial statements and the notes thereto included in the Company s annual report on Form 10-K for the year ended December 31, 2005 filed with the Securities and Exchange Commission (SEC) on March 16, 2006.

Significant Accounting Policies

The Company s significant accounting policies are disclosed in the Company s annual report on Form 10-K for the year ended December 31, 2005 and have not changed significantly as of September 30, 2006, with the exception of the following policies:

Stock-Based Compensation

Effective January 1, 2006, the Company adopted the fair value recognition provisions of Statement of Financial Accounting Standards (SFAS) No. 123 (revised 2004), Share-Based Payment (SFAS 123(R)), using the modified prospective transition method and therefore has not restated results for prior periods. Under this transition method, stock-based compensation expense for the first nine months of fiscal 2006 includes compensation expense for all stock-based compensation awards granted prior to, but not yet vested as of January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS No. 123, Accounting for Stock-Based Compensation (SFAS 123). Stock-based compensation expense for all stock-based compensation awards granted after January 1, 2006 is based on the grant-date fair value estimated in accordance with the provisions of SFAS 123(R). The Company recognizes these compensation costs on a straight-line basis over the requisite service period of the award, which is generally the vesting term of four years. Prior to the adoption of SFAS 123(R) the Company recognized stock-based compensation expense in accordance with Accounting Principles Board Opinion (APB) No. 25, Accounting for Stock Issued to Employees. In March 2005, the SEC issued Staff Accounting Bulletin (SAB) No. 107 *Share-Based Payment* regarding the SEC s interpretation of SFAS 123(R) and the valuation of stock-based payments for public companies. The Company has applied the provisions of SAB 107 in its adoption of SFAS 123(R). See Note 2 for a further discussion on stock-based compensation.

Intangible assets

Purchased technology licenses and other intangible assets are presented at cost, net of accumulated amortization. The technology licenses are being amortized on a straight-line basis over their expected useful life of 9-10 years and the other intangibles are being amortized over their expected useful life of two years.

Recent Accounting Pronouncements

In September 2006, the SEC issued SAB No. 108 regarding the process of quantifying financial statement misstatements. SAB No. 108 states that registrants should use both a balance sheet approach and an income statement approach when quantifying and evaluating the materiality of a misstatement. The interpretations in SAB No. 108 contain guidance on correcting errors under the dual approach as well as provide transition guidance for correcting errors. This interpretation does not change the requirements within SFAS No. 154, Accounting Changes and Error Corrections- a replacement of APB No. 20 and Financial Accounting Standards Board (FASB) Statement No. 3, for the correction of an error on financial statements. SAB No. 108 is effective for annual financial statements covering the first fiscal years ending after November 15, 2006. The Company will be required to adopt this interpretation by December 31, 2006. Management is currently evaluating the requirements of SAB No. 108 and the impact this interpretation may have on the consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements. This standard defines fair value, establishes a framework for measuring fair value in accounting principles generally accepted in the United States of America, and expands disclosure about fair value measurements. This pronouncement applies under other accounting standards that require or permit fair value measurements. Accordingly, this statement does not require any new fair value measurement. This statement is effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company will be required to adopt SFAS No. 157 in the first quarter of fiscal year 2008. Management is currently evaluating the requirements of SFAS No. 157 and has not yet determined the impact on the consolidated financial statements.

In July 2006, the FASB issued Interpretation No. 48, Accounting for Uncertainty in Income Taxes effective for fiscal years beginning after December 15, 2006. The Interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The Interpretation also provides guidance on derecognition, classification, interest and penalties, accounting for interim periods, disclosure, and transition. The Company will decide on its policy for interest and penalty classification by the end of 2006 and adopt the Interpretation beginning with the fiscal year ending 2007. Upon adoption, it is not expected that the Interpretation will have a material effect on the Company s financial position or results of operations.

Note 2. Accounting for Stock-Based Compensation

Periods Prior to the Adoption of SFAS 123(R)

Prior to January 1, 2006, the Company accounted for stock-based compensation under the recognition and measurement provisions of APB 25. Accordingly, the Company generally recognized compensation expense only when it granted options with a discounted exercise price. Any resulting compensation expense was recognized ratably over the associated service period, which was generally the option vesting term of four years. Effective January 1, 2006, the Company adopted SFAS 123(R), using the modified prospective application transition method, which requires the presentation of pro-forma information for periods prior to the adoption of SFAS 123(R) regarding the net income and net income per share as if the Company had accounted for its stock options under the fair value method of SFAS 123. For the purpose of this pro-forma disclosure, the estimated value of the stock awards is recognized on a straight line basis over the vesting periods of the awards. If compensation had been determined based upon the fair value at the grant date for employee compensation arrangements, consistent with the methodology prescribed in SFAS 123, the Company s pro-forma net income and pro-forma net income per share under SFAS 123 would have been as shown in the table below (in thousands, except per share data):

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	Three Months Ended September 30, 2005		Nine Months Ended September 30, 2005	
Net income, as reported	$	3,801	$	7,991
Add: Stock-based employee compensation expense included in reported net income, net of related tax effects		224		716
Less: Total stock-based employee compensation determined under fair-valued based method for all awards, net of related tax effects		(624)		(1,558)
Pro forma net income used in basic and diluted net income per share	$	3,401	$	7,149
Basic net income per share:				
As reported	$	0.33	$	0.70
Pro forma	$	0.29	$	0.63
Diluted net income per share:				
As reported	$	0.27	$	0.58
Pro forma	$	0.25	$	0.53

Stock Option Plans

As of September 30, 2006, the Company had the below mentioned stock-based employee compensation plans.

2004 Employee Stock Purchase Plan

The Company sponsors the 2004 Employee Stock Purchase Plan (2004 ESPP), pursuant to which eligible employees are permitted to purchase common stock at a discount through payroll deductions. The price of the common stock purchased is equal to 85% of the fair market value of the common stock at the beginning of an offering period or at the end of a purchase period. Shares of common stock eligible for p