

ENCISION INC
Form 10-Q
August 13, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

Form 10-Q

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

For the quarterly period ended June 30, 2013

OR

o 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: 001-11789

ENCISION INC.

(Exact name of registrant as specified in its charter)

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Colorado
(State or other jurisdiction of
incorporation or organization)

84-1162056
(I.R.S. Employer Identification No.)

6797 Winchester Circle

Boulder, Colorado 80301

(Address of principal executive offices)

(303) 444-2600

(Registrant's telephone number)

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 and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

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

Indicate the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date:

Common Stock, no par value
(Class)

8,210,100 Shares
(outstanding at July 31, 2013)

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ENCISION INC.

FORM 10-Q

For the Three Months Ended June 30, 2013

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Table of Contents**PART I** **FINANCIAL INFORMATION****ITEM 1 CONDENSED INTERIM FINANCIAL STATEMENTS****Encision Inc.****Condensed Balance Sheets****(unaudited)**

	June 30, 2013	March 31, 2013
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 94,268	\$ 126,224
Accounts receivable, net of allowance for doubtful accounts of \$16,000 at June 30, 2013 and \$9,000 at March 31, 2013	1,017,968	985,770
Inventories, net of reserve for obsolescence of \$55,000 at June 30, 2013 and \$51,000 at March 31, 2013	2,920,059	2,929,302
Prepaid expenses	182,309	65,891
Total current assets	4,214,604	4,107,187
Equipment, at cost:		
Furniture, fixtures and equipment	3,517,735	2,691,057
Customer-site equipment	1,003,111	931,060
Equipment-in-progress	56,075	774,004
Accumulated depreciation	(2,780,574)	(2,767,195)
Equipment, net	1,796,347	1,628,926
Patents, net of accumulated amortization of \$196,866 at June 30, 2013 and \$190,770 at March 31, 2013	243,902	237,606
Other assets	10,613	9,215
TOTAL ASSETS	\$ 6,265,466	\$ 5,982,934
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 442,221	\$ 823,347
Accrued compensation	315,871	319,116
Other accrued liabilities	443,454	446,171
Lease payable - short term	46,850	
Line of credit	725,000	
Total current liabilities	1,973,396	1,588,634
Lease payable - long term	121,676	
Total liabilities	2,095,072	1,588,634
Commitments and contingencies		
Shareholders' equity:		
Preferred stock, no par value: 10,000,000 shares authorized; none issued and outstanding		
Common stock and additional paid-in capital, no par value: 100,000,000 shares authorized; 8,210,100 shares issued and outstanding at June 30, 2013 and March 31, 2013		
	21,586,784	21,569,993
Accumulated (deficit)	(17,416,390)	(17,175,693)
Total shareholders' equity	4,170,394	4,394,300

TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	\$	6,265,466	\$	5,982,934
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The accompanying notes to financial statements are an integral part of these condensed statements.

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Encision Inc.

Condensed Statements of Operations

(Unaudited)

Three Months Ended	June 30, 2013	June 30, 2012
NET REVENUE:		
Product	\$ 2,618,930	\$ 2,805,351
Service	62,920	295,821
Total Revenue	2,681,850	3,101,172
COST OF REVENUE:		
Product	1,103,451	1,204,112
Service	50,002	148,720
Total Cost of Revenue	1,153,453	1,352,832
GROSS PROFIT	1,528,397	1,748,340
OPERATING EXPENSES:		
Sales and marketing	951,184	867,007
General and administrative	353,043	527,645
Research and development	388,087	342,746
Total operating expenses	1,692,314	1,737,398
OPERATING INCOME (LOSS)	(163,917)	10,942
Interest expense, net	(8,886)	(1,012)
Other income (expense), net	(67,894)	380
Interest expense and other income, net	(76,780)	(632)
INCOME (LOSS) BEFORE PROVISION FOR INCOME TAXES	(240,697)	10,310
Provision for income taxes		
NET INCOME (LOSS)	\$ (240,697)	\$ 10,310
Net income (loss) per share basic and diluted	\$ (0.03)	\$ 0.00
Weighted average shares basic	8,210,100	8,168,067
Weighted average shares diluted	8,210,100	8,177,853

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

Table of Contents**Encision Inc.****Condensed Statements of Cash Flows****(Unaudited)**

Three Months Ended	June 30, 2013	June 30, 2012
Cash flows from operating activities:		
Net income (loss)	\$ (240,697)	\$ 10,310
Adjustments to reconcile loss to net cash provided by operating activities:		
Depreciation and amortization	102,367	72,614
Stock-based compensation expense related to stock options	16,791	14,661
Provision for doubtful accounts, net	7,000	(11,000)
Provision for inventory obsolescence, net	4,000	8,000
Change in operating assets and liabilities:		
Accounts receivable	(39,198)	151,689
Inventories	5,243	103,419
Prepaid expenses and other assets	(117,816)	(124,092)
Accounts payable	(381,126)	(587,788)
Accrued compensation and other accrued liabilities	(5,962)	99,629
Net cash (used in) operating activities	(649,398)	(262,558)
Cash flows from investing activities:		
Acquisition of property and equipment	(95,166)	(65,768)
Patent costs	(12,392)	(5,905)
Net cash (used in) investing activities	(107,558)	(71,673)
Cash flows from financing activities:		
Borrowings from credit facility	725,000	
Proceeds from the issuance of common stock		255,000
Cost of the issuance of common stock		(22,286)
Net cash provided by financing activities	725,000	232,714
Net decrease in cash and cash equivalents	(31,956)	(101,517)
Cash and cash equivalents, beginning of period	126,224	564,671
Cash and cash equivalents, end of period	\$ 94,268	\$ 463,154

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

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ENCISION INC.

NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS

JUNE 30, 2013

(Unaudited)

Note 1. ORGANIZATION AND NATURE OF BUSINESS

Encision Inc. is a medical device company that designs, develops, manufactures and markets patented surgical instruments that provide greater safety to patients undergoing minimally-invasive surgery. We believe that our patented AEM® (Active Electrode Monitoring) surgical instrument technology is changing the marketplace for electrosurgical devices and instruments by providing a solution to a patient safety risk in laparoscopic surgery. Our sales to date have been made principally in the United States.

We have an accumulated deficit of \$17,416,390 at June 30, 2013. Operating funds have been provided primarily by issuances of our common stock and warrants, a line of credit, and the exercise of stock options to purchase our common stock. Should our liquidity be diminished in the future because of operating losses, we may be required to seek additional capital in the future. Our line of credit agreement with Silicon Valley Bank is subject to renewal in May 2014. There are no assurances that additional capital will be available to us on terms acceptable to us, or at all. These factors raise substantial doubt about our ability to continue as a going concern. Our ability to continue operations as a going concern, realize the carrying value of our assets, and discharge our liabilities in the normal course of business is dependent upon our ability to generate profitable operations, and if needed, the ability to raise substantial capital sufficient to fund our commitments and ongoing losses.

Our strategic marketing and sales plan is designed to expand the use of our products in surgically active hospitals and surgery centers in the United States.

Note 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation. The condensed interim financial statements included herein have been prepared by us, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles accepted in the United States (GAAP) have been condensed or omitted pursuant to such rules and regulations, although we believe that the disclosures made are adequate to make the information presented not misleading. The condensed interim financial statements and notes thereto should be read in conjunction with the financial statements and the notes thereto included in our Annual Report on Form 10-K for the fiscal year ended March 31, 2013, filed on June 28, 2013.

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The accompanying condensed interim financial statements have been prepared, in all material respects, in conformity with the standards of accounting measurements and reflect, in the opinion of management, all adjustments necessary to summarize fairly the financial position and results of operations for such periods in accordance with GAAP. All adjustments are of a normal recurring nature. The results of operations for the most recent interim period are not necessarily indicative of the results to be expected for the full year.

Use of Estimates in the Preparation of Financial Statements. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions. Such estimates and assumptions affect the reported amounts of assets and liabilities as well as disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of sales and expense during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents. For purposes of reporting cash flows, we consider all cash and highly liquid investments with an original maturity of three months or less to be cash equivalents.

Fair Value of Financial Instruments. Our financial instruments consist of cash and cash equivalents, short-term trade receivables and payables and a line of credit. The carrying values of cash and cash equivalents, short-term trade receivables and payables approximate their fair value due to their short maturities. The interest rate associated with the line of credit is variable and based upon fluctuations of the prime rate, thus the carrying value approximates fair value.

Concentration of Credit Risk. Financial instruments, which potentially subject us to concentrations of credit risk, consist of cash and cash equivalents, accounts receivable and a line of credit. The amount of cash on deposit with financial institutions may exceed the \$250,000 federally insured limit at June 30, 2013. We believe that cash on deposit that exceeds \$250,000 with financial institutions is financially sound and the risk of loss is minimal.

We have no significant off-balance sheet concentrations of credit risk such as foreign exchange contracts, options contracts or other foreign hedging arrangements. We maintain the majority of our cash balances with one financial institution in the form of demand deposits.

Accounts receivable are typically unsecured and are derived from transactions with and from entities in the healthcare industry primarily located in the United States. Accordingly, we may be exposed to credit risk generally associated with the healthcare industry. We maintain allowances for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. The net accounts receivable balance at June 30, 2013 of \$1,017,968 included 3% from one customer. The net accounts receivable balance at March 31, 2013 of \$985,770 included 6% from one customer.

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Warranty Accrual. We provide for the estimated cost of product warranties at the time sales are recognized. While we engage in extensive product quality programs and processes, including actively monitoring and evaluating the quality of our component suppliers, our warranty obligation is based upon historical experience and is also affected by product failure rates and material usage incurred in correcting a product failure. Should actual product failure rates or material usage costs differ from our estimates, revisions to the estimated warranty liability would be required.

Inventories. Inventories are stated at the lower of cost (first-in, first-out basis) or market. We reduce inventory for estimated obsolete or unmarketable inventory equal to the difference between the cost of inventory and the estimated market value based upon assumptions about future demand and market conditions. If actual market conditions are less favorable than those projected by management, additional inventory write-downs may be required. At June 30, 2013 and March 31, 2013, inventory consisted of the following:

	June 30, 2013		March 31, 2013
Raw materials	\$ 1,744,344	\$	1,843,357
Finished goods	1,230,715		1,136,945
Total gross inventories	2,975,059		2,980,302
Less reserve for obsolescence	(55,000)		(51,000)
Total net inventories	\$ 2,920,059	\$	2,929,302

Property and Equipment. Property and equipment are stated at cost, with depreciation computed over the estimated useful lives of the assets, generally three to seven years. We use the straight-line method of depreciation for property and equipment. Leasehold improvements are depreciated over the shorter of the remaining lease term or the estimated useful life of the asset. Maintenance and repairs are expensed as incurred and major additions, replacements and improvements are capitalized.

Long-Lived Assets. Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. A long-lived asset is considered impaired when estimated future cash flows related to the asset, undiscounted and without interest, are insufficient to recover the carrying amount of the asset. If deemed impaired, the long-lived asset is reduced to its estimated fair value. Long-lived assets to be disposed of are reported at the lower of their carrying amount or estimated fair value less cost to sell.

Patents. The costs of applying for patents are capitalized and amortized on a straight-line basis over the lesser of the patent's economic or legal life (20 years from the date of application in the United States). Capitalized costs are expensed if patents are not issued. We review the carrying value of our patents periodically to determine whether the patents have continuing value and such reviews could result in the conclusion that the recorded amounts have been impaired.

Income Taxes. We account for income taxes under the provisions of FASB Accounting Standards Codification (ASC) Topic 740, Accounting for Income Taxes (ASC 740). ASC 740 requires recognition of deferred income tax assets and liabilities for the expected future income tax consequences, based on enacted tax laws, of temporary differences between the financial reporting and tax bases of assets and liabilities. ASC 740 also requires recognition of deferred tax assets for the expected future tax effects of all deductible temporary differences, loss carryforwards and tax credit carryforwards. Deferred tax assets are then reduced, if deemed necessary, by a valuation allowance for the amount of any tax benefits which, more likely than not based on current circumstances, are not expected to be realized. As a result, no provision for income tax is reflected in the accompanying statements of operations. Should we achieve sufficient, sustained income in the future, we may conclude that some or all of the valuation allowance should be reversed. We are required to make many subjective assumptions and judgments regarding our income tax exposures. At June 30, 2013, we had no unrecognized tax benefits, which would affect the effective tax rate if recognized and had no

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accrued interest, or penalties related to uncertain tax positions.

Revenue Recognition. Revenue from product sales is recorded when we ship the product and title has passed to the customer, provided that we have evidence of a customer arrangement and can conclude that collection is probable. Our shipping policy is FOB Shipping Point. We recognize revenue from sales to stocking distributors when there is no right of return, other than for normal warranty claims. We have no ongoing obligations related to product sales, except for normal warranty obligations. Revenue from engineering services is recognized when the service is performed.

Research and Development Expenses. We expense research and development costs for products and processes as incurred.

Stock-Based Compensation. Stock-based compensation is presented in accordance with the guidance of ASC Topic 718, Compensation - Stock Compensation (ASC 718). Under the provisions of ASC 718, companies are required to estimate the fair value of share-based payment awards on the date of grant using an option-pricing model. The value of the portion of the award that is ultimately expected to vest is recognized as expense over the requisite service periods in our statements of operations.

Stock-based compensation expense recognized under ASC 718 for the three months ended June 30, 2013 and 2012 was \$16,791 and \$14,661, respectively, which consisted of stock-based compensation expense related to grants of employee stock options.

Segment Reporting. We have concluded that we have one operating segment.

Recent Accounting Pronouncements. We have reviewed all recently issued, but not yet effective, accounting pronouncements and do not believe the future adoption of any such pronouncements may be expected to cause a material impact on our financial condition or the results of our operations.

Note 3. BASIC AND DILUTED INCOME AND LOSS PER COMMON SHARE

We report both basic and diluted net income (loss) per share. Basic net income or loss per common share is computed by dividing net income or loss for the period by the weighted average number of common shares outstanding for the period. Diluted net income or loss per common share is computed by dividing the net income or loss for the period by the weighted average number of common and potential common shares outstanding during the period if the effect of the potential common shares is dilutive. The shares used in the calculation of dilutive potential common shares exclude options to purchase shares where the exercise price was greater than the average market price of common shares for the period.

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The following table presents the calculation of basic and diluted net loss per share:

	Three Months Ended	
	June 30, 2013	June 30, 2012
Net income (loss)	\$ (240,697)	\$ 10,310
Weighted-average shares basic	8,210,100	8,168,067
Effect of dilutive potential common shares		9,786
Weighted-average shares diluted	8,210,100	8,177,853
Net income (loss) per share basic	\$ (0.03)	\$ 0.00
Net income (loss) per share diluted	\$ (0.03)	\$ 0.00
Antidilutive employee stock options	547,000	735,214

Note 4. COMMITMENTS AND CONTINGENCIES

We currently lease our facilities at 6797 Winchester Circle, Boulder, Colorado under noncancelable lease agreements through July 31, 2014. The minimum future lease payment, by fiscal year, as of June 30, 2013 is as follows:

Fiscal Year	Amount
2014 (nine months remaining)	\$ 240,060
2015	108,303
Total	\$ 348,363

Our minimum future capital equipment lease payments with General Electric Capital Corporation as of June 30, 2013, by fiscal year, are as follows:

Fiscal Year	Amount
2014 (nine months remaining)	\$ 57,155
2015	76,207
2016	53,470
2017	4,283
Total	191,115
Less portion representing interest	(23,351)
Present value of minimum lease payment	167,764
Less current portion	(46,850)
	\$ 120,914

Included in our furniture, fixtures and equipment balance is leased equipment that was acquired, under the provisions of a long-term capital lease, during the quarter ended June 30, 2013. The equipment had an original cost of \$177,547 and has a net book value of \$166,439 at June 30, 2013.

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On May 10, 2012, we signed an amendment to our credit facility agreement with Silicon Valley Bank, effective May 10, 2012. The terms of the credit facility include a line of credit for \$2,000,000 for two years at an interest rate calculated at the prime rate plus 1.25%, subject to increase upon a default. Our borrowing under the credit facility is limited by our eligible receivables and inventory at the time of borrowing. The credit facility is secured by all tangible and intangible assets, whether now owned or hereafter acquired, wherever located. As of June 30, 2013, under our eligible receivables and inventory limit, we had an additional \$369,000 available to borrow. Our credit facility agreement with Silicon Valley Bank requires us to meet certain financial covenants. During our quarter ended June 30, 2013, we failed to meet the minimum defined quick debt ratio covenant. As a result, the lender may impose a monthly maintenance fee, requires additional financial reporting and restricts our borrowings to the beginning of each week instead of when needed.

Aside from the operating and capital leases, we do not have any material contractual commitments requiring settlement in the future.

We are subject to regulation by the United States Food and Drug Administration (FDA). The FDA provides regulations governing the manufacture and sale of our products and regularly inspects us and other manufacturers to determine compliance with these regulations. We believe that we were in substantial compliance with all known regulations as of June 30, 2013. FDA inspections are conducted periodically at the discretion of the FDA. Our latest inspection by the FDA occurred in December 2012.

Note 5. SHARE-BASED COMPENSATION

The provisions of ASC 718-10-55 requires the measurement and recognition of compensation expense for all share-based payment awards made to our employees and directors, including employee stock options, based on estimated fair values. The following table summarizes stock-based compensation expense related to employee stock options and employee stock purchases for the three months ended June 30, 2013 and 2012, which was allocated as follows:

	Three Months Ended	
	June 30, 2013	June 30, 2012
Cost of sales	\$ 345	\$ 685
Sales and marketing	1,899	