MISONIX INC
Form 10-Q
November 09, 2011

FORM 10-Q

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

(Mark One)

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

For the quarterly period ended September 30, 2011

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: 1-10986

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

New York (State or other jurisdiction of incorporation or organization)	11-2148932 (I.R.S. Employer Identification No.)
1938 New Highway, Farmingdale, NY (Address of principal executive offices)	11735 (Zip Code)

(631) 694-9555
(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 þ No o

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. (Check one):

Accelerated filer o Non-accelerated filer o

Large accelerated filer o		Smaller reporting company þ
	(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 þ

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

Class of Common Stock	Outstanding at November 9, 2011
Common Stock, $.01 par value	7,001,370

MISONIX, INC.

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PART I — FINANCIAL INFORMATION

Item 1. Financial Statements.

MISONIX, INC. and Subsidiaries
Consolidated Balance Sheets

	September 30, 2011 (Unaudited)	June 30, 2011 (Derived from audited financial statements)
Assets		
Current assets:		
Cash and cash equivalents	$ 6,206,855	$ 6,881,093
Accounts receivable, less allowance for doubtful accounts of $130,739 and $115,739, respectively	2,050,526	2,294,254
Inventories, net	3,879,875	3,779,020
Prepaid expenses and other current assets	267,854	374,472
Note receivable	460,000	210,000
Total current assets	12,865,110	13,538,839
Property, plant and equipment, net	1,069,395	991,195
Goodwill	1,701,094	1,701,094
Other assets	1,807,818	2,127,194
Total assets	$ 17,443,417	$ 18,358,322
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	1,971,100	1,336,558
Other accrued expenses and other current liabilities	1,230,143	1,969,078
Total current liabilities	3,201,243	3,305,636
Deferred lease liability	16,281	14,043
Deferred income	150,307	161,360
Total liabilities	3,367,831	3,481,039
Commitments and contingencies		
Stockholders' equity:		
Common stock, $.01 par value-shares authorized 20,000,000, 7,079,170 issued, and 7,001,370 outstanding	70,792	70,792
Additional paid-in capital	25,870,205	25,787,960
Acculated deficit	(11,452,987)	(10,569,045)
Treasury stock, at cost, 77,800 shares	(412,424)	(412,424)
Total stockholders' equity	14,075,586	14,877,283
Total liabilities and stockholders' equity	$ 17,443,417	$ 18,358,322

See Accompanying Notes to Consolidated Financial Statements.

MISONIX, INC. and Subsidiaries
Consolidated Statements of Operations
(Unaudited)

	For the three months ended September 30, 2011	2010
Net sales	$ 3,739,156	$ 3,257,988
Cost of goods sold	1,817,477	1,620,703
Gross profit	1,921,679	1,637,285
Operating expenses:		
Selling expenses	1,270,407	965,007
General and administrative expenses	1,167,820	1,217,805
Research and development expenses	397,226	460,494
Total operating expenses	2,835,453	2,643,306
Loss from operations	(913,774)	(1,006,021)
Other income (expense):		
Interest income	19	50
Interest expense	(212)	(3,641)
Royalty income and license fees	138,135	179,115
Royalty expense	(28,570)	(19,343)
Other	(14,546)	45,409
Total other income	94,826	201,590
Loss from continuing operations before income taxes	(818,948)	(804,431)
Income tax expense	4,960	38,100
Net loss from continuing operations	(823,908)	(842,531)
Discontinued operations:		
Net loss from discontinued operations net of tax of $0 and $0, respectively	(60,034)	(175,315)
Total net loss from discontinued operations	(60,034)	(175,315)
Net loss	$ (883,942)	$ (1,017,846)
Net loss per share from continuing operations – Basic	$ (0.12)	$ (0.12)
Net loss per share from discontinued operations – Basic	(0.01)	(0.03)
Net loss per share – Basic	$ (0.13)	$ (0.15)
Net loss per share from continuing operations – Diluted	$ (0.12)	$ (0.12)
Net loss per share from discontinued operations – Diluted	(0.01)	(0.03)
Net loss per share – Diluted	$ (0.13)	$ (0.15)
Weighted Average Shares – Basic	7,001,370	7,001,370
Weighted Average Shares – Diluted	7,001,370	7,001,370

See Accompanying Notes to Consolidated Financial Statements.

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MISONIX, INC. and Subsidiaries
Consolidated Statement of Stockholders' Equity
(Unaudited)

For the three months ended
September 30, 2011

	Common Stock $.01 Par value		Treasury Stock				
	Number of shares	Amount	Number of shares	Amount	Additional paid-in capital	Accumulated deficit	Total stockholders' equity
Balance, June 30, 2011	7,079,170	$70,792	(77,800)	$(412,424)	$25,787,960	$(10,569,045)	$14,877,283
Net loss\comprehensive loss	-	-	-	-	-	(883,942)	(883,942)
Stock-based compensation	-	-	-	-	82,245	-	82,245
Balance, September 30, 2011	7,079,170	$70,792	(77,800)	$(412,424)	$25,870,205	$(11,452,987)	$14,075,586

See Accompanying Notes to Consolidated Financial Statements.

MISONIX, INC. and Subsidiaries
Consolidated Statements of Cash Flows
(Unaudited)

	For the three months ended September 30, 2011	2010
Operating activities		
Net loss from continuing operations	$ (823,908)	$ (842,531)
Adjustments to reconcile net loss to net cash used in continuing operating activities:		
Depreciation and amortization and other non-cash items	175,065	35,972
Bad debt expense (recovery)	15,000	(31,022)
Loss on disposal of property, plant and equipment	-	(18,515)
Stock-based compensation	82,245	60,106
Deferred income	(34,774)	(36,008)
Deferred lease liability	2,238	1,404
Changes in operating assets and liabilities:		
Accounts receivable	228,728	425,892
Inventories	29,025	(218,969)
Prepaid expenses and other current assets	106,618	(96,143)
Accounts payable and accrued expenses	(76,872)	(110,427)
Other	12,188	233,137
Net cash used in operating activities	(284,447)	(597,104)
Investing activities		
Acquisition of property, plant and equipment	(196,077)	(26,927)
Deferred payment on asset acquisition	(129,880)	-
Net cash used in investing activities	(325,957)	(26,927)
Financing activities		
Payments of short-term borrowings	-	(93,188)
Principal payments on capital lease obligations	(3,800)	(3,557)
Net cash used in financing activities	(3,800)	(96,745)
Cash flows from discontinued operations		
Net cash used in operating activities	(60,034)	(175,315)
Net cash provided by investing activities	-	405,000
Net cash (used) provided by discontinued operations	(60,034)	229,685
Effect of exchange rate changes on cash	-	3,923
Net decrease in cash and cash equivalents	(674,238)	(487,168)
Cash and cash equivalents at beginning of period	6,881,093	9,900,605
Cash and cash equivalents at end of period	$ 6,206,855	$ 9,413,437
Supplemental disclosure of cash flow information:		
Cash paid for:		
Interest	$ 212	$ 3,641
Income taxes	$ 5,903	$ 42,100

See Accompanying Notes to Consolidated Financial Statements.

MISONIX, INC. and Subsidiaries
Notes to Consolidated Financial Statements
(Unaudited)

1. Basis of Presentation

The accompanying unaudited financial information should be read in conjunction with the audited consolidated financial statements and the notes thereto included in our Annual Report on Form 10-K for the year ended June 30, 2011 ("2011 Annual Report"). A summary of the Company's significant accounting policies is identified in Note 1 of the notes to the consolidated financial statements included in the Company's 2011 Annual Report. There have been no changes in the Company's significant accounting policies subsequent to June 30, 2011.

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X pursuant to the requirements of the U.S. Securities and Exchange Commission. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. The results of operations for the interim periods are not necessarily indicative of the results of operations for the entire year.

The consolidated financial statements of MISONIX, INC. ("Misonix" or the "Company") include the accounts of Misonix and its 100% owned subsidiaries, Misonix Limited and Hearing Innovations, Inc. ("Hearing Innovations"). All significant intercompany balances and transactions have been eliminated.

Organization and Business

Misonix is a New York corporation which, through its predecessors, was first organized in 1959. The Company designs, manufactures, develops and markets minimally invasive ultrasonic medical device products. These products include the BoneScalpelTM cutting system which is used among other things for surgical procedures of the spine, the SonaStar® Surgical Aspirator which is used to emulsify and remove soft and hard tumors, the SonicOne® Wound Cleansing and Debridement System (“SonicOne”) that offers tissue specific debridement and cleansing of wounds for effective removal of devitalized tissue and fibrin deposits while sparing viable cells, and the AutoSonix ultrasound cutting and coagulating system which is marketed by Misonix through an agreement with Covidien Ltd. Misonix also markets its Lysonix ultrasound assisted liposuction device through Mentor Corporation, a subsidiary of Johnson & Johnson (“Mentor”). The Company also develops and markets ductless fume enclosures for filtration of gaseous contaminates in the laboratory and forensic markets.

For the quarter ended September 30, 2011 and 2010, approximately 38% and 27%, respectively, of the Company's net sales were to foreign markets. Sales by the Company in other major industrial countries are made primarily through distributors.

Hearing Innovations is located in Farmingdale, New York and is a development company with patented HiSonic ultrasonic technology for the treatment of profound deafness and tinnitus.

Discontinued Operations

On August 4, 2009, the Company sold its Labcaire Systems, Ltd. ("Labcaire") subsidiary to PuriCore International Limited ("PuriCore Limited") for a total purchase price of up to $5.6 million. The Company received $3.6 million at closing and a promissory note in the principal amount of $1 million, payable in equal installments of $250,000 on the next four anniversaries of the closing. During the year ended June 30, 2011, the Company received the first installment. The note receivable was discounted over the four years using a 4% imputed interest rate. This rate was consistent with published discounts. The discounted value of the note ($900,000) was used to determine gain or loss on the sale and the remaining outstanding balance is included in other assets in the consolidated balance sheet, with the current portion reflected as a component of notes receivable. The Company was also to receive a commission paid on sales for the period commencing on the date of closing and ending on December 31, 2013 of 8% of the pass through Automated Endoscope Reprocessing ("AER") and Drying Cabinet products, and 5% of license fees from any chemical licenses marketed by Labcaire directly associated with sale of AERs, specifically for the disinfection of the endoscope. The aggregate commission payable to the Company was also to be subject to a maximum payment of $1,000,000. The aggregate commission was not recognized in determining the gain or loss on the sale of Labcaire until the commission was to be paid. As of June 30, 2011, there were no commissions paid. For the year ended June 30, 2010, the Company recorded a pre-tax loss on the sale of Labcaire of $295,879. Results of Labcaire operations have been reported as a discontinued operation for all periods presented.

In January 2011, PuriCore Limited initiated a lawsuit against the Company in the High Court of Justice, Queens Bench Division, Commercial Court, Royal Courts of Justice, London, England (Claim No. 2011-42) (the "Lawsuit"). In the Lawsuit, PuriCore Limited claimed damages from the Company in respect of breach of warranties contained in the Stock Purchase Agreement, dated August 4, 2009 (the "SPA"), pursuant to which the Company sold Labcaire to PuriCore Limited. PuriCore Limited claimed damages of £2,167,000 or approximately $3,600,000, plus interest and its legal costs. The Company denied the allegations contained in the Lawsuit.

On July 19, 2011, PuriCore Limited and the Company reached an agreement to settle the Lawsuit (the "Settlement"). The Settlement provides that the Company (i) forgive in full PuriCore Limited and PuriCore plc's obligation under the SPA to pay up to $1,000,000 of the previously unrecorded, contingent commissions (as described above); (ii) pay PuriCore, Inc. ("PuriCore"), an affiliate of PuriCore Limited, $650,000 towards PuriCore Limited's legal costs which had been accrued for as of June 30, 2011 and recorded as a component of loss from discontinued operations for the year ended June 30, 2011 and (iii) enter into a Product License and Distribution Agreement, dated as of July 19, 2011, with PuriCore (the "Distribution Agreement").

MISONIX, INC. and Subsidiaries
Notes to Consolidated Financial Statements
(Unaudited)

Pursuant to the Distribution Agreement, the Company has been granted the right to distribute PuriCore's Vashe solution products in the United States, on a private label basis, as an irrigating solution for the treatment of human wound care in conjunction with therapeutic ultrasonic procedures (the "Field"). PuriCore has agreed, subject to modification, not to sell the products that are the subject of the Distribution Agreement (the "Licensed Products") to any other therapeutic ultrasound company for distribution in the Field in the United States ("Exclusivity"). The Company has agreed not to sell or distribute in the United States in the Field any irrigating solution that has anti-microbial properties other than the Licensed Products so long as the Company has Exclusivity.

The Distribution Agreement is for a three (3) year term with automatic renewals for successive two (2) year periods; provided that the Company and PuriCore have agreed upon sales volume targets for each renewal period (such volume targets not to increase by more than ten (10%) percent year over year unless otherwise agreed) and provided that the cost terms shall be no less favorable than the twelve (12) months leading up to the start of such renewal period. In no event will the Distribution Agreement survive beyond the expiration or invalidation of all of PuriCore's patents.

During the initial term of the Distribution Agreement, the Company is obligated to either purchase or pay a minimum of $2,000,000 in gross margin value to PuriCore for the Licensed Products (the "Minimum Payment"). The Minimum Payment is subject to downward adjustment and elimination in the event that (i) PuriCore chooses to eliminate Exclusivity, (ii) the Company's right to manufacture the Licensed Products under certain conditions has been triggered but the Company is unable to manufacture the Licensed Products or to have the Licensed Products manufactured for it by third parties or (iii) the U.S. Food and Drug Administration has made a final determination that prohibits the sale of the Licensed Products for use in the Field.

The Company has the right to manufacture the Licensed Products if PuriCore is unable to meet certain performance standards and will pay PuriCore a royalty after the $2,000,000 in gross margin value requirement has been satisfied if the Company is then manufacturing the Licensed Products.

During a renewal period, PuriCore may terminate the Distribution Agreement if (i) the Company fails to purchase the agreed upon volume target for such renewal period and does not cure such failure in accordance with the Distribution Agreement or (ii) upon twelve (12) months’ notice.

MISONIX, INC. and Subsidiaries
Notes to Consolidated Financial Statements
(Unaudited)

The following represents predominantly legal and other expenses associated with Labcaire and Misonix HIFU Technologies Limited which are included in discontinued operations:

	For the three months ended September 30, 2011	2010
Revenues	$ -	$ -
(Loss) from discontinued operations, before tax	$ (60,034)	$ (175,315)
Income tax expense	-	-
Loss from discontinued operations net of tax	$ (60,034)	$ (175,315)

Accounts Receivable

Accounts receivable, principally trade, are generally due within 30 to 90 days and are stated at amounts due from customers, net of an allowance for doubtful accounts. The Company performs ongoing credit evaluations and adjusts credit limits based upon payment history and the customer's current credit worthiness, as determined by a review of their current credit information. The Company continuously monitors aging reports, collections and payments from customers and maintains a provision for estimated credit losses based upon historical experience and any specific customer collection issues that have been identified. While such credit losses have historically been within expectations and the provisions established, the Company cannot guarantee that the same credit loss rates will be experienced in the future. The Company writes off accounts receivable when they become uncollectible.

Reclassifications

Certain prior period amounts in the accompanying financial statements and related notes have been reclassified to conform to the current period's presentation.

2. Net Income (Loss) Per Share of Common Stock

Basic net income (loss) per common share ("basic EPS") is computed by dividing net income (loss) by the weighted average number of common shares outstanding for the period. Diluted net loss per common share ("diluted EPS") is computed by dividing net income (loss) by the weighted average number of common shares and dilutive common share equivalents outstanding (principally outstanding common stock options) for the period.

The number of weighted average common shares used in the calculation of basic EPS and diluted EPS were as follows:

	For the three months ended September 30, 2011	2010
Basic shares	7,001,370	7,001,370
Dilutive effect of stock options	—	—
Diluted shares	7,001,370	7,001,370

Diluted EPS for the three months ended September 30, 2011 and September 30, 2010 presented is the same as basic EPS, as the inclusion of the effect of common share equivalents then outstanding would be anti-dilutive. For this reason, excluded from the calculation of diluted EPS are outstanding options to purchase 2,029,165 and 2,010,560 shares of common stock for the three months ended September 30, 2011 and September 30, 2010, respectively.

3. Comprehensive Loss

Total comprehensive loss was $883,942 for three months ended September 30, 2011 and $1,017,846 for the three months ended September 30, 2010, respectively. There are no components of comprehensive loss other than net loss for all periods presented.

4. Stock-Based Compensation

Stock options are granted with exercise prices not less than the fair market value of our common stock at the time of the grant, with an exercise term (as determined by the committee administering the applicable option plan (the "Committee")) not to exceed 10 years. The Committee determines the vesting period for the Company's stock options. Generally, such stock options have vesting periods of immediate to four years. Certain option awards provide for accelerated vesting upon meeting specific retirement, death or disability criteria, and upon a change in control. During the three month periods ended September 30, 2011 and 2010, the Company granted options to purchase 233,750 and 219,500 shares of the Company's common stock, respectively.

Stock-based compensation expense for the three month periods ended September 30, 2011 and 2010 was $82,000 and $60,000, respectively. Compensation expense is recognized in the general and administrative expenses line item of the Company's statements of operations on a straight-line basis over the vesting periods. As of September 30, 2011, there was approximately $960,000 of total unrecognized compensation cost related to non-vested stock-based compensation arrangements to be recognized over a weighted-average period of 3.1 years.

MISONIX, INC. and Subsidiaries
Notes to Consolidated Financial Statements
(Unaudited)

There was no cash received from the exercise of stock options for three month periods ended September 30, 2011 and 2010. Cash flows from tax benefits attributable to tax deductions in excess of the compensation cost recognized for those options (excess tax benefits) are classified as financing cash flows.

The fair values of the options granted during the periods ended September 30, 2011 and 2010 were estimated on the date of the grant using the Black-Scholes option-pricing model on the basis of the following weighted average assumptions during the respective periods:

	For the three months ended September 30,					
		2011			2010	
Risk-free interest rate		3.4	%		3.9	%
Expected option life in years		6.5			6.5	
Expected stock price volatility		75.4	%		78.3	%
Expected dividend yield		0.0	%		0.0	%
Weighted-average fair value of options granted	$	1.75		$	1.49	

The expected life was based on historical exercises and terminations. The expected volatility for the expected life of the options is determined using historical price changes of the Company's stock over a period equal to that of the expected life of the options. The risk free rate is based upon the U.S. Treasury yield in effect at the time of the grant. The expected dividend yield is 0% as the Company has historically not declared dividends and does not expect to declare any in the future.

Changes in outstanding stock options during the three months ended September 30, 2011 were as follows:

	Options			
	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (years)	Aggregate Intrinsic Value (a)
Outstanding as of June 30, 2011	1,795,415	4.06		
Granted	233,750	2.19		
Forfeited	—			
Expired	—			
Outstanding as of September 30, 2011	2,029,165	3.84	5.9	$49,527
Exercisable and vested at September 30, 2011	1,398,565	4.62	4.7	$18,727
Available for grant at September 30, 2011	432,950			

(a) Intrinsic value for purposes of this table represents the amount by which the fair value of the underlying stock, based on the respective market prices at September 30, 2011 or if exercised, the exercise dates, exceeds the exercise prices of the respective options.

5. Income Taxes

There are no federal, state or foreign income tax audits in process as of September 30, 2011. Open tax years related to federal and state income tax filings are for the years ended June 30, 2008, 2009, 2010 and 2011. The Company files state tax returns in New York and Colorado and its tax returns in those states have never been examined. The Company's foreign subsidiaries, Misonix Limited and Misonix Urology Services Limited (formerly, UKHIFU Limited) file tax returns in England. The England Inland Revenue Service has not examined these tax returns. Misonix Sarl files tax returns in France. The French tax authorities have not examined these tax returns. As of September 30, 2011 and June 30, 2011, the Company has no material unrecognized tax benefits.

As of September 30, 2011, the valuation allowance was determined by estimating the recoverability of the deferred tax assets. In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. In making this assessment, the ultimate realization of deferred tax assets is dependent upon the generation of future taxable income and tax planning strategies in making this assessment. Based on these considerations, management concluded that it is more likely than not that its deferred tax assets will not be fully realized.