

EMAGIN CORP  
Form 10-Q  
November 19, 2007

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

**Form 10-Q**

(Mark One)

**R QUARTERLY REPORT UNDER SECTION 13 OR 15(D) OF THE  
SECURITIES EXCHANGE ACT OF 1934**

**For the quarterly period ended September 30, 2007  
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 001-15751**

**eMAGIN CORPORATION**

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

**Delaware**

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

**56-1764501**

*(I.R.S. Employer  
Identification No.)*

**10500 NE 8<sup>th</sup> Street, Suite 1400, Bellevue, Washington 98004**

*(Address of principal executive offices)*

**(425) 749-3600**

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

**Securities registered pursuant to Section 12(b) of the Act: None**

**Securities registered pursuant to Section 12(g) of the Act: Common Stock, \$.001 Par Value Per Share**

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 R 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 £

Non-accelerated filer R

Edgar Filing: EMAGIN CORP - Form 10-Q

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

The number of shares of common stock outstanding as of October 31, 2007 was 12,620,900.

1

---

**eMagin Corporation**  
**Form 10-Q**  
**For the Quarter ended September 30, 2007**

**Table of Contents**

		<b>Page</b>
<b>PART I FINANCIAL INFORMATION</b>		
Item 1	Condensed Consolidated Financial Statements	
	Condensed Consolidated Balance Sheets as of September 30, 2007 (unaudited) and December 31, 2006	3
	Condensed Consolidated Statements of Operations for the Three and Nine months ended September 30, 2007 and 2006 (unaudited)	4
	Condensed Consolidated Statements of Changes in Shareholders' Capital Deficit for the Nine months ended September 30, 2007 (unaudited)	5
	Condensed Consolidated Statements of Cash Flows for the Nine months ended September 30, 2007 and 2006 (unaudited)	6
	Notes to Condensed Consolidated Financial Statements (unaudited)	7
Item 2	Management's Discussion and Analysis of Financial Condition and Results of Operations	15
Item 3	Quantitative and Qualitative Disclosures About Market Risk	19
Item 4	Controls and Procedures	19
<b>PART II OTHER INFORMATION</b>		
Item 1	Legal Proceedings	21
Item 1A	Risk Factors	21
Item 2	Unregistered Sales of Equity Securities and Use of Proceeds	26
Item 3	Defaults Upon Senior Securities	27
Item 4	Submission of Matters to a Vote of Security Holders	27
Item 5	Other Information	27

Item 6	Exhibits	27
--------	----------	----

<b>SIGNATURES</b>		28
-------------------	--	----

**CERTIFICATIONS**

**ITEM 1. Condensed Consolidated Financial Statements**

**eMAGIN CORPORATION**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
(In thousands, except share data)

	<b>September 30, 2007 (unaudited)</b>	<b>December 31, 2006</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 792	\$ 1,415
Investments – held to maturity	138	171
Accounts receivable, net	2,698	908
Inventory	1,951	2,485
Prepaid expenses and other current assets	801	656
Total current assets	6,380	5,635
Equipment, furniture and leasehold improvements, net	365	666
Intangible assets, net	52	55
Other assets	231	233
Deferred financing costs, net	40	416
Total assets	\$ 7,068	\$ 7,005
<b>LIABILITIES AND SHAREHOLDERS' CAPITAL DEFICIT</b>		
Current liabilities:		
Accounts payable	\$ 1,188	\$ 1,192
Accrued compensation	1,349	959
Other accrued expenses	881	749
Advance payments	396	444
Deferred revenue	254	126
Current portion of capitalized lease obligations	—	6
Current portion of debt	657	1,217
Derivative liability - warrants	—	1,195
Other current liabilities	68	52
Total current liabilities	4,793	5,940
Long-term debt	5,931	2,229
Total liabilities	10,724	8,169
Commitments and contingencies		
Shareholders' capital deficit:		
Preferred stock, \$.001 par value: authorized 10,000,000 shares; no shares issued and outstanding	—	—

Edgar Filing: EMAGIN CORP - Form 10-Q

Series A Senior Secured Convertible Preferred stock, stated value \$1,000 per share, \$.001 per value: 3,198 shares designated, and none issued.

Common stock, \$.001 par value: authorized 200,000,000 shares, issued and outstanding, 12,224,556 shares as of September 30, 2007 and 10,341,029 shares as of December 31, 2006

	12	10
Additional paid-in capital	194,473	179,651
Accumulated deficit	(198,141)	(180,825)
Total shareholders' capital deficit	(3,656)	(1,164)
Total liabilities and shareholders' capital deficit	\$ 7,068	\$ 7,005

See notes to Condensed Consolidated Financial Statements.

**eMAGIN CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
(In thousands, except share and per share data)  
(unaudited)

	<b>Three Months Ended</b>		<b>Nine months</b>	
	<b>September 30,</b>		<b>Ended September 30,</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Revenue:				
Product revenue	\$ 4,318	\$ 2,242	\$ 11,985	\$ 5,487
Contract revenue	753	50	927	120
Total revenue, net	5,071	2,292	12,912	5,607
Cost of goods sold	3,059	2,940	9,120	8,934
Gross profit (loss)	2,012	(648)	3,792	(3,327)
Operating expenses:				
Research and development	564	965	2,304	3,507
Selling, general and administrative	1,434	1,838	5,198	6,674
Total operating expenses	1,998	2,803	7,502	10,181
Income (loss) from operations	14	(3,451)	(3,710)	(13,508)
Other income (expense):				
Interest expense	(592)	(509)	(2,766)	(509)
Loss on extinguishment of debt	(10,749)	—	(10,749)	—
Gain (loss) on warrant derivative liability	(1,496)	177	(853)	177
Other income, net	172	14	762	73
Total other (expense) income	(12,665)	(318)	(13,606)	(259)
Net loss	\$ (12,651)	\$ (3,769)	\$ (17,316)	\$ (13,767)
Loss per share, basic and diluted	\$ (1.06)	\$ (0.37)	\$ (1.53)	\$ (1.37)
Weighted average number of shares outstanding:				
Basic and diluted	11,934,705	10,077,260	11,300,757	10,030,988

See notes to Condensed Consolidated Financial Statements.





**eMAGIN CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' CAPITAL DEFICIT**  
(In thousands)

	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Accumulated Deficit	Total Shareholders' Deficit
Balance, December 31, 2006	10,341	\$ 10	\$ 179,651	\$ (180,825)	\$ (1,164)
Stock-based compensation	—	—	1,172	—	1,172
Debt conversion to equity	797	1	309	—	310
Issuance of common stock for services	1,076	1	952	—	953
Exercise of common stock warrants	10	—	3	—	3
Expiration of derivative liability- warrants	—	—	2,653	—	2,653
Beneficial conversion premium	—	—	5,078	—	5,078
Fair value of warrants issued	—	—	4,655	—	4,655
Net loss	—	—	—	(17,316)	(17,316)
Balance, September 30, 2007 (unaudited)	12,224	\$ 12	\$ 194,473	\$ (198,141)	\$ (3,656)

See notes to Condensed Consolidated Financial Statements.

**eMAGIN CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(In thousands)

	<b>Nine months Ended</b>	
	<b>September 30,</b>	
	<b>2007</b>	<b>2006</b>
	<b>(unaudited)</b>	
Cash flows from operating activities:		
Net loss	\$ (17,316)	\$ (13,767)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	313	792
Amortization of deferred financing fees	266	—
Reduction of provision for sales returns and doubtful accounts	(35)	(18)
Stock-based compensation	1,172	2,270
Issuance of common stock for services	953	375
Amortization of discount on notes payable	1,848	382
Gain on warrant derivative liability	853	(177)
Loss on extinguishment of debt	10749	—
Changes in operating assets and liabilities:		
Accounts receivable	(1,755)	(339)
Inventory	534	899
Prepaid expenses and other current assets	(145)	(8)
Deferred revenue	128	20
Accounts payable, accrued compensation, other accrued expenses, and advanced payments	750	(899)
Other current liabilities	15	101
Net cash used in operating activities	(1,670)	(10,369)
Cash flows from investing activities:		
Purchase of equipment	(9)	(204)
Proceeds from or (purchase of) investments – held to maturity	33	(4)
Purchase of intangibles and other assets	—	(2)
Net cash provided by (used in) investing activities	24	(210)
Cash flows from financing activities:		
Proceeds from exercise of stock options and warrants	3	10
Proceeds from long-term debt and line of credit	1,108	5,379
Payments related to deferred financing costs	(40)	—
Payments of long-term debt and capital leases	(48)	(130)
Net cash provided by financing activities	1,023	5,259
Net decrease in cash and cash equivalents	(623)	(5,320)
Cash and cash equivalents beginning of period	1,415	6,727
Cash and cash equivalents end of period	\$ 792	\$ 1,407
Cash paid for interest	\$ 281	\$ 127
Cash paid for taxes	\$ 67	\$ 35

During the nine months ended September 30, 2007, the Company:

Entered into an intellectual property agreement with Kodak where Kodak was assigned the rights to a specific patent and as part of the consideration waived the royalty payments for the first six months of 2007 and reduced the royalty

payment to 50% for the third quarter. \$723 thousand was recorded as income from the licensing of intangible assets; Issued approximately 797 thousand shares for the conversion of Notes and interest totaling approximately \$310 thousand; and

Entered into amended Note Purchase Agreement with investors and issued warrants that are exercisable at \$1.03 per share into approximately 5.4 million shares of common stock.

See notes to Condensed Consolidated Financial Statements.

**eMAGIN CORPORATION**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(Unaudited)**

**Note 1: Description of the Business and Summary of Significant Account Policies**

***The Business***

eMagin Corporation is a developer and manufacturer of optical systems and microdisplays for use in the electronics industry. eMagin also develops and markets microdisplay systems and optics technology for commercial, industrial and military applications.

***Basis of Presentation***

In the opinion of management, the accompanying unaudited condensed consolidated financial statements of eMagin Corporation and its subsidiary reflects all adjustments, including normal recurring accruals, necessary for a fair presentation. Certain information and footnote disclosure normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted pursuant to instruction, rules and regulations prescribed by the Securities and Exchange Commission. The Company believes that the disclosures provided herein are adequate to make the information presented not misleading when these unaudited condensed consolidated financial statements are read in conjunction with the audited consolidated financial statements contained in the Company's Annual Report on Form 10-K for the year ended December 31, 2006. The results of operations for the period ended September 30, 2007 are not necessarily indicative of the results to be expected for the full year.

On November 3, 2006, the Company effected a one-for-ten (1-for-10) reverse stock split of its issued and outstanding common stock. All common and per share amounts in the accompanying financial statements have been adjusted to reflect the 1-for-10 reverse stock split.

The condensed consolidated financial statements have been prepared assuming that the Company will continue as a going concern. The Company has had recurring losses from operations which it believes will continue through the foreseeable future. The Company's cash requirements over the next twelve months are greater than the Company's cash, cash equivalents, and investments at September 30, 2007. The Company has a shareholders' deficit at September 30, 2007. These factors raise substantial doubt regarding the Company's ability to continue as a going concern. The condensed consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty. To address the liquidity issue, the Company entered into an asset based loan agreement in August 2007 establishing a \$2.5 million revolving line of credit. See Note 7 for additional information.

***Use of Estimates***

The preparation of financial statements in conformity with generally accepted accounting principles in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements as well as the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. These estimates and assumptions relate to recording net revenue, collectibility of accounts receivable, useful lives and impairment of tangible and intangible assets, accruals, derivative liability, income taxes, inventory realization and other factors. Management has exercised reasonable judgment in deriving these estimates. Consequently, a change in conditions could affect these estimates.

***Revenue Recognition***

Revenue is recognized when products are shipped to customers, net of allowances for anticipated returns. The Company's revenue-earning activities generally involve delivering products, and revenues are considered to be earned when the Company has completed the process by which it is entitled to such revenues. Revenue is recognized when persuasive evidence of an arrangement exists, delivery has occurred, selling price is fixed or determinable and collection is reasonably assured. The Company defers revenue recognition on products sold directly to the consumer with a fifteen day right of return. Revenue is recognized upon the expiration of the right of return.