RITA MEDICAL SYSTEMS INC
Form 10-Q
May 10, 2005
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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 March 31, 2005

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 000-30959

RITA MEDICAL SYSTEMS, INC.

(Exact name of registrant as specified in its charter)

Delaware	**94-3199149**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

46421 Landing Parkway

Fremont, CA 94538

(Address of principal executive offices, including zip code)

510-771-0400

(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 an accelerated filer (as defined in Rule 12b-2 of the Act). Yes x No ¨

As of April 29, 2005, there were 41,496,759 shares of the registrant s common stock outstanding.

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PART 1. FINANCIAL INFORMATION

Item 1. Financial Statements

RITA MEDICAL SYSTEMS, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, unaudited)

	March 31, 2005	December 31, 2004
Assets		
Current assets:		
Cash and cash equivalents	$ 5,906	$ 12,978
Marketable securities	251	880
Accounts and note receivable, net	6,480	6,410
Inventories	6,881	7,126
Prepaid and other current assets	1,219	792
Total current assets	20,737	28,186
Long term note receivable, net	140	177
Property and equipment, net	1,865	1,966
Goodwill	91,339	91,339
Intangible assets	29,885	30,600
Other assets	139	41
Total assets	$ 144,105	$ 152,309
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	$ 3,700	$ 2,572
Accrued liabilities	2,929	4,159
Current portion of long term debt	708	7,200
Total current liabilities	7,337	13,931
Long term debt, less current portion	9,452	9,632
Other long term liabilities	82	90
Total liabilities	16,871	23,653
Stockholders equity		
Common stock	41	41

Additional paid-in capital	217,158	216,893
Accumulated other comprehensive loss		(2)
Accumulated deficit	(89,965)	(88,276)
Total stockholders equity	127,234	128,656
Total liabilities and stockholders equity	$ 144,105	$ 152,309

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

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RITA MEDICAL SYSTEMS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data, unaudited)

	Three months ended March 31,	
	2005	**2004**
Sales	$ 11,205	$ 4,644
Cost of goods sold	4,805	1,615
Gross profit	6,400	3,029
Operating expenses:		
Research and development	1,039	843
Selling, general and administrative	6,768	4,366
Restructuring charges	60	
Total operating expenses	7,867	5,209
Loss from operations	(1,467)	(2,180)
Interest expense	(287)	
Interest income and other expense, net	65	10
Net loss	$ (1,689)	$ (2,170)
Net loss per common share, basic and diluted	$ (0.04)	$ (0.12)
Shares used in computing net loss per common share, basic and diluted	41,457	17,998

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

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RITA MEDICAL SYSTEMS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands, unaudited)

	Three months ended March 31,	
	2005	**2004**
Cash flows from operating activities:		
Net loss	$ (1,689)	$ (2,170)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	970	410
Loss on disposal of property and equipment		13
Amortization of stock-based compensation		107
Allowance for (recovery of) doubtful accounts receivable	(178)	27
Provision for obsolete inventories	101	86
Changes in operating assets and liabilities:		
Accounts and note receivable	108	(43)
Inventories	144	329
Prepaid and other current assets	(427)	232
Accounts payable and accrued liabilities	(102)	(439)
Deferred maintenance revenue	(4)	2
Net cash used in operating activities	(1,077)	(1,446)
Cash flows from investing activities:		
Purchase of property and equipment	(154)	(98)
Purchase of marketable securities	(60)	(404)
Sales and maturities of marketable securities	691	3,770
Note receivable, other assets and other long term liabilities	(65)	23
Net cash provided by investing activities	412	3,291
Cash flows from financing activities:		
Principal payments on debt	(6,672)	
Proceeds from issuance of common stock, net of issuance costs	265	97
Net cash provided by (used in) financing activities	(6,407)	97
Net decrease in cash and cash equivalents	(7,072)	1,942
Cash and cash equivalents at beginning of period	12,978	3,780
Cash and cash equivalents at end of period	$ 5,906	$ 5,722

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

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RITA MEDICAL SYSTEMS, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of presentation

The accompanying unaudited condensed consolidated financial statements have been prepared by RITA Medical Systems, Inc. (the Company) in accordance with accounting principles generally accepted in the United States of America for interim financial information. These principles are consistent in all material respects with those applied in the Company s financial statements contained in the Company s annual report on Form 10-K for the fiscal year ended December 31, 2004, as amended, and pursuant to the instructions to Form 10-Q and Article 10 of Regulation S-X promulgated by the Securities and Exchange Commission. However, interim financial statements do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain all adjustments (all of which are of a normal recurring nature, including the elimination of intercompany accounts) necessary to present fairly the financial position, results of operations and cash flows of the Company for the periods indicated. Interim results of operations are not necessarily indicative of the results to be expected for the full year or any other interim periods. These unaudited condensed consolidated financial statements should be read in conjunction with the financial statements and footnotes thereto for the year ended December 31, 2004 contained in the Company s annual report on Form 10-K.

2. Business Combination

On July 29, 2004, the Company merged with Horizon Medical Products, Inc. (Horizon) in a transaction accounted for under the purchase method of accounting. None of Horizon s results of operations prior to that date are included in the Company s condensed consolidated statements of operations. However, the Company has prepared pro forma financial information showing sales and net loss for the combined entity for the three month period ended March 31, 2004, as if the merger occurred as of January 1, 2004. This unaudited pro forma financial information is presented below in comparison to the Company s unaudited sales and net loss for the three month period ended March 31, 2005, but is not intended to represent or be indicative of the consolidated results of operations of the Company that would have been reported had the acquisition been completed as of January 1, 2004, and should not be taken as representative of the future consolidated results of operations or financial condition of the Company (in thousands, except per share amounts):

	Three months ended March 31,	
	Actual 2005	**Pro forma 2004**
Sales	$ 11,205	$ 11,730
Net loss	$ (1,689)	$ (3,528)
Net loss per common share, basic and diluted	$ (0.04)	$ (0.10)

Restructuring costs of $1,369,000, consisting entirely of severance related to the termination of employees to eliminate certain duplicative activities, have been incurred since completion of the merger. Of this amount, $60,000 was incurred during the three months ended March 31, 2005 (see Note 11, Restructuring).

3. Liquidity

As of March 31, 2005, the Company s total assets were $144.1 million, total tangible assets were $22.9 million, total liabilities were $16.9 million, working capital was $13.4 million and cash, cash equivalents and marketable securities totaled $6.2 million. Current and anticipated demand for the Company s products as well as procurement and production affect the need for capital. Changes in these or other factors could have a material impact on capital requirements and may require the Company to raise additional capital. While the Company believes that its existing cash resources, including marketable securities, will be sufficient to fund its operating needs for the next twelve months, additional financing may be required for the Company s currently envisioned long term needs. If the Company needs to raise additional financing, it will seek to sell additional equity or debt securities, obtain an additional credit facility or renegotiate debt repayment terms. There can be no assurance that any additional financing will be available on terms acceptable to the Company, or at all. In addition, future equity financings could result in dilution to shareholders, and future debt financings could result in certain financial and operational restrictions. Failure to obtain sufficient funds on acceptable terms when needed, to make timely debt payments, or to achieve our growth or profitability objectives may require us to curtail operations, perhaps to a significant extent.

4. Reclassifications

Certain prior year balances have been reclassified to conform to current year presentation. In the Company s quarterly report on Form 10-Q for the three month period ended March 31, 2004, investments in variable rate debt obligations with interest rate reset

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intervals of less than 90 days were classified as cash equivalents. The Company s Consolidated Statement of Cash Flows for the three months ended March 31, 2004 has been modified from past presentation to give effect to purchases and sales or maturities of such securities in the determination of net cash provided by investing activities. For the three months ended March 31, 2004, net cash provided by investing activities increased by $400,000. The Company s Consolidated Statements of Operations and Comprehensive Loss for the three months ended March 31, 2005 and 2004 were not affected by this reclassification.

5. Net loss per share

Basic earnings per share figures are calculated based on the weighted-average number of common shares outstanding during the period less the weighted-average number of any common shares subject to repurchase by the Company. Diluted earnings per share further include the dilutive effect of potentially dilutive securities consisting of stock options and warrants provided that the inclusion of such securities is not antidilutive; the Company has reported net losses and therefore has excluded such potentially dilutive securities from its calculation of diluted earnings per share. The following numbers of shares represented by stock options and warrants (prior to application of the treasury stock method) were excluded from the computation of diluted net loss per share as their effect was antidilutive (in thousands):

	March 31,	
	2005	**2004**
Effect of potentially dilutive securities:		
Options	7,256	2,743
Warrants	78	25
Total potentially dilutive securities excluded from the computation of net loss per common share as their effect was antidilutive	7,334	2,768

6. Accounting for stock-based compensation

During the year ended December 31, 2002, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 148, Accounting for Stock-Based Compensation Transition and Disclosure. The Company accounts for stock-based employee compensation arrangements in accordance with provisions of Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees and Financial Accounting Standards Board Interpretations (FIN) No. 28, Accounting for Stock Appreciation Rights and Other Variable Stock Option or Award Plans.

Under APB Opinion No. 25, compensation expense is based on the difference, if any, on the date of the grant between the fair value of the Company s stock and the exercise price. SFAS No. 123 defines a fair value based method of accounting for an employee stock option or similar equity instruments.

The following table illustrates the effect on net loss and net loss per common share for the three month periods ended March 31, 2005 and 2004, respectively, if the Company had applied the fair value recognition provisions of SFAS No. 123 to stock-based employee compensation granted under all of its stock option plans and its Employee Stock Purchase Plan (in thousands, except per share amounts):

	Three months ended March 31,	
	2005	2004
Net loss, as reported	$ (1,689)	$ (2,170)
Add: Stock-based employee compensation expense included in reported net loss		107
Deduct: Total stock-based employee compensation determined under the fair value based method for all awards	(518)	(809)
Net loss, pro-forma	$ (2,207)	$ (2,872)
Basic and diluted net loss per common share:		
As reported	$ (0.04)	$ (0.12)
Pro-forma	$ (0.05)	$ (0.16)

The determination of stock-based employee compensation, as relating to stock option plans, under the fair value based method used the following weighted average assumptions:

	Three months ended March 31,	
	2005	2004
Volatility	78%	75%
Risk-free interest rate	3.83%	3.13%
Expected life	5 years	