ACCURAY INC
Form 10-Q
May 09, 2013
Table of Contents

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 March 31, 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: 001-33301

ACCURAY INCORPORATED

(Exact Name of Registrant as Specified in Its Charter)

Delaware	**20-8370041**
(State or Other Jurisdiction of Incorporation or Organization)	(IRS Employer Identification Number)

1310 Chesapeake Terrace

Sunnyvale, California 94089

(Address of Principal Executive Offices Including Zip Code)

(408) 716-4600

(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 reports), and (2) has been subject to such filing requirements for the past 90 days. x Yes o 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 (§ 229.405 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 x No o

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 definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o	Accelerated filer x
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

As of April 30, 2013, there were 74,115,872 shares of the Registrant s Common Stock, par value $0.001 per share, outstanding.

Accuray Incorporated

Form 10-Q for the Quarter Ended March 31, 2013

Table of Contents

		Page No.
PART I.	**Financial Information**	3
Item 1.	Condensed Consolidated Financial Statements (Unaudited)	3
	Condensed Consolidated Balance Sheets as of March 31, 2013 and June 30, 2012	3
	Condensed Consolidated Statements of Operations and Comprehensive Loss for the three and nine months ended March 31, 2013 and 2012	4
	Condensed Consolidated Statements of Cash Flows for the nine months ended March 31, 2013 and 2012	5
	Notes to Condensed Consolidated Financial Statements	6
Item 2.	Management s Discussion and Analysis of Financial Condition and Results of Operations	17
Item 3.	Quantitative and Qualitative Disclosures About Market Risk	25
Item 4.	Controls and Procedures	25
PART II.	**Other Information**	27
Item 1.	Legal Proceedings	27
Item 1A.	Risk Factors	27
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds	32
Item 3.	Defaults Upon Senior Securities	32
Item 4.	Mine Safety Disclosures	32
Item 5.	Other Information	32
Item 6.	Exhibits	32
Signatures		34

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

Accuray Incorporated

Condensed Consolidated Balance Sheets

(in thousands, except share and per share amounts)

(Unaudited)

	March 31, 2013	June 30, 2012 (1)
Assets		
Current assets:		
Cash and cash equivalents	$ 181,526	$ 143,504
Restricted cash	2,613	1,560
Accounts receivable, net of allowance for doubtful accounts of $1,383 and $1,700, respectively	53,992	67,890
Inventories	92,225	81,693
Prepaid expenses and other current assets	15,869	16,715
Deferred cost of revenue - current	7,345	4,896
Total current assets	353,570	316,258
Property and equipment, net	35,325	37,458
Goodwill	59,368	59,215
Intangible assets, net	34,102	49,819
Deferred cost of revenue - noncurrent	2,295	2,433
Other assets	12,418	7,987
Total assets	$ 497,078	$ 473,170
Liabilities and equity		
Current liabilities:		
Accounts payable	$ 14,982	$ 18,209
Accrued compensation	15,456	23,071
Other accrued liabilities	26,323	31,646
Customer advances - current	16,114	18,177
Deferred revenue - current	91,091	83,071
Total current liabilities	163,966	174,174
Long-term liabilities:		
Long-term other liabilities	4,322	5,988
Deferred revenue - noncurrent	9,087	9,675
Long-term debt	197,658	79,466
Total liabilities	375,033	269,303
Commitment and contingencies (Note 5)		
Equity:		
Preferred stock, $0.001 par value; authorized: 5,000,000 shares; no shares issued and outstanding		
Common stock, $0.001 par value; authorized: 200,000,000 and 100,000,000 shares at March 31, 2013 and June 30, 2012, respectively; issued and outstanding: 74,096,245 and	74	72

71,864,268 shares at March 31, 2013 and June 30, 2012, respectively		
Additional paid-in capital	420,511	409,143
Accumulated other comprehensive income	2,391	2,837
Accumulated deficit	(300,931)	(216,427)
Total stockholders equity	122,045	195,625
Non-controlling interest		8,242
Total equity	122,045	203,867
Total liabilities and equity	$ 497,078	$ 473,170

(1) The condensed consolidated balance sheet at June 30, 2012 has been derived from audited consolidated financial statements.

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

Table of Contents

Accuray Incorporated

Condensed Consolidated Statements of Operations and Comprehensive Loss

(in thousands, except per share amounts)

(Unaudited)

	Three Months Ended March 31, 2013	Three Months Ended March 31, 2012	Nine Months Ended March 31, 2013	Nine Months Ended March 31, 2012
Net revenue:				
Products	$ 25,023	$ 59,875	$ 98,821	$ 179,851
Services	45,524	41,720	132,253	127,218
Other		221		1,621
Total net revenue	70,547	101,816	231,074	308,690
Cost of revenue:				
Cost of products	18,403	32,401	60,976	103,574
Cost of services	32,091	33,100	99,743	103,626
Cost of other		204		708
Total cost of revenue	50,494	65,705	160,719	207,908
Gross profit	20,053	36,111	70,355	100,782
Operating expenses:				
Selling and marketing	12,646	12,449	41,296	40,047
Research and development	15,697	22,398	51,510	59,799
General and administrative	16,745	13,964	45,479	42,047
Total operating expenses	45,088	48,811	138,285	141,893
Loss from operations	(25,035)	(12,700)	(67,930)	(41,111)
Other expense, net	(5,565)	(838)	(8,849)	(8,074)
Loss before provision for income taxes	(30,600)	(13,538)	(76,779)	(49,185)
Provision for income taxes	603	1,247	1,867	2,152
Loss from continuing operations	(31,203)	(14,785)	(78,646)	(51,337)
Loss from discontinued operations (Note 9):				
Loss from operations of a discontinued variable interest entity		(1,748)	(3,505)	(5,470)
Impairment of indefinite lived intangible asset of discontinued variable interest entity			(12,200)	
Loss from deconsolidation of a variable interest entity			(3,442)	
Loss from discontinued operations, net of tax of $0		(1,748)	(19,147)	(5,470)
Loss from discontinued operations attributable to non-controlling interest		(1,652)	(13,289)	(5,029)
Loss from discontinued operations attributable to stockholders		(96)	(5,858)	(441)
Net loss attributable to stockholders	$ (31,203)	$ (14,881)	$ (84,504)	$ (51,778)
Loss per share attributable to stockholders				
Basic and diluted - continuing operations	$ (0.42)	$ (0.21)	$ (1.08)	$ (0.73)
Basic and diluted - discontinued operations	$	$ (0.00)	$ (0.08)	$ (0.00)
Basic and diluted - net loss	$ (0.42)	$ (0.21)	$ (1.16)	$ (0.73)

Weighted average common shares used in computing loss per share								
Basic and diluted		74,016		71,120		72,953		70,692
Net loss attributable to stockholders	$	(31,203)	$	(14,881)	$	(84,504)	$	(51,778)
Foreign currency translation adjustment		(82)		(617)		(446)		1,750
Comprehensive loss	$	(31,285)	$	(15,498)	$	(84,950)	$	(50,028)

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

Table of Contents

Accuray Incorporated

Condensed Consolidated Statements of Cash Flows

(in thousands)

(Unaudited)

	Nine Months Ended March 31, 2013	2012
Cash Flows From Operating Activities		
Loss from continuing operations	$ (78,646)	$ (51,337)
Loss from discontinued operations	(19,147)	(5,470)
Adjustments to reconcile net loss to net cash used in operating activities		
Depreciation and amortization	19,845	24,512
Impairment of indefinite lived intangible asset	12,200	
Share-based compensation	6,119	6,301
Accretion of interest on long-term debt	3,192	2,590
Provision for (recovery of) bad debt	(317)	997
Provision for write-down of inventories	1,718	2,007
Loss on disposal of property and equipment	585	245
Gain on previously held equity interest in Morphormics	(662)	
Loss from deconsolidation of a variable interest entity	3,442	
Changes in assets and liabilities:		
Restricted cash	(1,050)	(285)
Accounts receivable	13,238	(12,942)
Inventories	(12,248)	9,242
Prepaid expenses and other assets	693	4,368
Deferred cost of revenue	(2,333)	563
Accounts payable	(2,197)	(15,803)
Accrued liabilities	(12,313)	(15,577)
Customer advances	(2,185)	(6,333)
Deferred revenue	8,125	24,135
Net cash used in operating activities	(61,941)	(32,787)
Cash Flows From Investing Activities		
Purchases of property and equipment, net	(11,621)	(7,714)
Purchase of intangible asset	(232)	
Acquisition of business, net of cash acquired	(3,861)	(1,384)
Net cash used in investing activities	(15,714)	(9,098)
Cash Flows From Financing Activities		
Proceeds from issuance of common stock	5,555	2,704
Proceeds from debt, net of costs	110,462	96,100
Net cash provided by financing activities	116,017	98,804
Effect of exchange rate changes on cash and cash equivalents	(340)	(1,497)
Net increase in cash and cash equivalents	38,022	55,422
Cash and cash equivalents at beginning of period	143,504	95,906
Cash and cash equivalents at end of period	$ 181,526	$ 151,328

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

5

Table of Contents

Accuray Incorporated

Notes to Condensed Consolidated Financial Statements

(Unaudited)

1. Summary of Significant Accounting Policies

Description of Business

Accuray Incorporated (together with its subsidiaries, the Company or Accuray) is incorporated in Delaware. The Company designs, develops and sells advanced radiosurgery and radiation therapy systems for the treatment of tumors throughout the body.

Basis of Presentation and Principles of Consolidation

The condensed consolidated financial statements include the accounts of the Company, its wholly-owned subsidiaries and a variable interest entity, Compact Particle Acceleration Corporation (CPAC) until its deconsolidation on December 21, 2012 (for further information, see Note 9, Investment in CPAC). All significant inter-company transactions and balances have been eliminated in consolidation.

The accompanying condensed consolidated financial statements have been prepared in accordance with United States generally accepted accounting principles, (GAAP), pursuant to the rules and regulations of the Securities and Exchange Commission (the SEC). Certain information and note disclosures have been condensed or omitted pursuant to such rules and regulations. The unaudited condensed consolidated financial statements have been prepared on the same basis as the annual financial statements and, in the opinion of management, reflect all adjustments, which include only normal recurring adjustments, necessary for a fair presentation of the periods presented. The results for the three and nine months ended March 31, 2013 are not necessarily indicative of the results to be expected for the year ending June 30, 2013, for any other interim period or for any future year.

Use of Estimates

The preparation of condensed consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosures at the date of the financial statements. Key estimates and assumptions made by the Company relate to revenue recognition, business combinations and intangible asset impairment, inventories, share-based compensation expense, income taxes, loss contingencies and corporate bonus expenses and accruals. Actual results could differ materially from those estimates.

Concentration of Credit and Other Risks

The Company s cash and cash equivalents are mainly deposited with several major financial institutions. At times, deposits in these institutions exceed the amount of insurance provided on such deposits. The Company has not experienced any losses in such accounts and believes that it is not exposed to any significant risk on these balances.

For the three and nine months ended March 31, 2013 and 2012, there were no customers that represented 10% or more of total net revenue. At March 31, 2013 and June 30, 2012, there was one customer and two customers, respectively, whose accounts receivable balances were 10% or more of the Company s total accounts receivable.

Accounts receivable are typically not collateralized. The Company performs ongoing credit evaluations of its customers and maintains reserves for potential credit losses. Accounts receivable are deemed past due in accordance with the contractual terms of the agreement. Accounts are charged against the allowance for doubtful accounts once collection efforts are unsuccessful. Historically, such losses have been within management s expectations.

Single source suppliers presently provide the Company with several components. In most cases, if a supplier was unable to deliver these components, the Company believes that it would be able to find other sources for these components subject to any regulatory qualifications, if required.

Revenue Recognition

The Company earns revenue from the sale of products, the operation of its shared ownership program, and the provision of related services, which include post-contract customer support (PCS), installation services, training and other professional services. The Company records its revenues net of any value added or sales tax. For arrangements with multiple elements, the Company allocates arrangement fees to product and services based upon Vendor Specific Objective Evidence of fair value of the respective elements, or Third-Party Evidence, or Best Estimate of Selling Price using the relative selling price method.

Table of Contents

Product Revenue

The majority of product revenue is normally generated from sales of CyberKnife and TomoTherapy systems. The Company sells its systems with PCS contracts, installation services, training, and at times, professional services. PCS contracts provide planned and corrective maintenance services, software updates, bug fixes, as well as call-center support. If the Company is responsible for installation, the Company recognizes revenue after installation and acceptance of the system; otherwise, revenue is recognized upon delivery.

Service Revenue

Service revenue is generated primarily from PCS (warranty period services and post warranty services), installation services, training, and professional services. PCS revenue is deferred and recognized over the service period. Installation service revenue is recognized concurrent with system revenue. Training and professional service revenues that are not deemed essential to the functionality of the systems are recognized as such services are performed.

Costs associated with service revenue are expensed when incurred, except when those costs are related to system upgrades where revenue recognition has been deferred. In those cases, the incremental costs are deferred and are recognized over the period of revenue recognition.

Shared ownership program

The Company also enters into arrangements under its shared ownership program with certain customers. These arrangements typically have a term of five years and provide the customer an option to purchase the system during the contractual term at pre-determined prices. Under the terms of this program, the Company retains title to its system, while the customer has use of the system. The Company generally receives a minimum monthly payment and earns additional revenues from the customer based upon its use of the system which are included in product revenue in the condensed consolidated statements of operations and comprehensive loss.

Other revenue

Other revenue primarily consists of research and development and construction contract revenues.

Long-term construction and manufacturing contracts

The Company recognizes revenue and cost of revenue related to long-term construction and manufacturing contracts using contract accounting on the percentage-of-completion or the completed contract method. The Company records such revenue under other revenue and cost of such revenue under cost of other revenue in the condensed consolidated statements of operations and comprehensive loss. Any loss provision identified from the total contract in the period is recorded as an increase to cost of revenue.

Loss Per Share

Basic and diluted loss per share is computed by dividing loss attributable to stockholders by the weighted average number of common shares outstanding during the period. The potential dilutive shares of the Company s common stock resulting from the assumed exercise of outstanding stock options, the vesting of Restricted Stock Units (RSUs), Market Stock Units (MSUs) and Performance-based Stock Units (PSUs), and the purchase of shares under the Employee Stock Purchase Plan (ESPP), as determined under the treasury stock method, are excluded from the computation of diluted loss per share because their effect would have been anti-dilutive.

A reconciliation of the numerator and denominator used in the calculation of basic and diluted loss per share attributable to stockholders follows (in thousands):

	Three Months Ended March 31, 2013	Three Months Ended March 31, 2012	Nine Months Ended March 31, 2013	Nine Months Ended March 31, 2012
Numerator:				
Loss from operations used in computing loss per share from continuing operations	$ (31,203)	$ (14,785)	$ (78,646)	$ (51,337)
Loss from discontinued operations used in computing loss per share from discontinued operations	$	$ (96)	$ (5,858)	$ (441)
Net loss used in computing net loss per share	$ (31,203)	$ (14,881)	$ (84,504)	$ (51,778)
Denominator:				
Weighted average shares used in computing basic loss per share	74,016	71,120	72,953	70,692
Add: Dilutive stock options and awards outstanding				
Weighted average shares used in computing diluted loss per share	74,016	71,120	72,953	70,692

Table of Contents

The 3.75% Convertible Senior Notes due August 1, 2016 (the 3.75% Convertible Notes) and the 3.50% Convertible Senior Notes due February 1, 2018 (the 3.50% Convertible Notes) are included in the calculation of diluted loss per share if their inclusion is dilutive under the if-converted method. The following table sets forth all potentially dilutive securities excluded from the computation in the table above because their effect would have been anti-dilutive (in thousands):

	As of March 31, 2013	As of March 31, 2012
Stock options	5,257	7,925
RSUs, MSUs and PSUs	3,321	2,097
3.75% Convertible Notes	10,560	10,560
3.50% Convertible Notes	21,576	
	40,714	20,582

Segment Information

The Company has determined that it operates in only one segment, as it only reports profit and loss information on an aggregate basis to its chief operating decision maker. The Company s long-lived assets maintained outside the United States are not material. Revenue by geographic region is based on the shipping addresses of the Company s customers. The following summarizes revenue by geographic region (in thousands):

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2013	2012	2013	2012
Americas	$ 28,372	$ 46,655	$ 99,262	$ 149,766
Europe, Middle East, India and Africa	25,290	25,825	78,246	79,770
Asia (excluding Japan)	8,496	17,059	29,154	52,931
Japan	8,389	12,277	24,412	26,223
Total	$ 70,547	$ 101,816	$ 231,074	$ 308,690

Recent Accounting Pronouncements

In February 2013, the Financial Accounting Standards Board issued Accounting Standards Update No. 2013-02, *Comprehensive Income (Topic 220) Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income* (ASU 2013-02), to improve the reporting of reclassifications out of accumulated other comprehensive income. ASU 2013-02 requires an entity to report the effect of significant reclassifications out of accumulated other comprehensive income on the respective line items in net income if the amount being reclassified is required under GAAP to be reclassified in its entirety to net income. For other amounts that are not required under GAAP to be reclassified in their entirety from accumulated other comprehensive income to net income in the same reporting period, an entity is required to cross-reference other disclosures required under GAAP that provide additional detail about those amounts. ASU 2013-02 is effective for the Company in its first quarter of fiscal 2014 with earlier adoption permitted, which should be applied prospectively. The Company does not expect that adoption of this guidance during fiscal 2014 will have a material impact on the Company s consolidated financial position, results of operations or cash flows.

2. Balance Sheet Components

Accounts receivable, net

Accounts receivable, net consisted of the following (in thousands):

	March 31, 2013	June 30, 2012
Accounts receivable	$ 54,970	$ 69,285
Unbilled fees and services	405	305
	55,375	69,590
Less: Allowance for doubtful accounts	(1,383)	(1,700)
Accounts receivable, net	$ 53,992	$ 67,890

Table of Contents

Financing receivables

A financing receivable is a contractual right to receive money, on demand or on fixed or determinable dates, that is recognized as an asset in the creditor s balance sheet. The Company s financing receivables, consisting of its accounts receivable with contractual maturities of more than one year totaled $3.0 million and $2.5 million at March 31, 2013 and June 30, 2012, respectively and are included in Other Assets in the condensed consolidated balance sheets. There was no balance in the allowance for doubtful accounts related to such financing receivables as of March 31, 2013 and June 30, 2012, respectively.

Inventories

Inventories consisted of the following (in thousands):

	March 31, 2013	June 30, 2012
Raw materials	$ 37,780	$ 34,579
Work-in-process	24,729	16,547
Finished goods	29,716	30,567
Inventories	$ 92,225	$ 81,693

Property and equipment, net

Property and equipment, net consisted of the following (in thousands):

	March 31, 2013	June 30, 2012
Furniture and fixtures	$ 6,495	$ 5,921
Computer and office equipment	9,166	9,126
Software	9,420	9,429
Leasehold improvements	19,301	16,065
Machinery and equipment	37,173	33,493
Shared ownership systems	4,979	4,979
Construction in progress	1,241	3,787
	87,775	82,800
Less: Accumulated depreciation	(52,450)	(45,342)
Property and equipment, net	$ 35,325	$ 37,458

Depreciation expense related to property and equipment for the three and nine months ended March 31, 2013 was $3.7 million and $11.6 million, respectively. Depreciation expense related to property and equipment for the three and nine months ended March 31, 2012 was $4.0 million and $12.3 million, respectively.

3. Goodwill and Intangible Assets

Goodwill

Activity related to goodwill consisted of the following (in thousands):

	Nine Months Ended March 31, 2013	Year Ended June 30, 2012
Balance at the beginning of the period	$ 59,215	$ 54,474
Addition related to acquisition	77	
Currency translation and other adjustments	76	
Adjustments related to prior year acquisition (1)		4,741
Balance at the end of the period	$ 59,368	$ 59,215

(1) Primarily represents liabilities related to the TomoTherapy acquisition.

Table of Contents

Intangible Assets

The Company s intangible assets associated with completed acquisitions at March 31, 2013 and June 30, 2012 are as follows (in thousands):

		March 31, 2013			June 30, 2012		
	Useful Lives (in years)	**Gross Carrying Amount**	**Accumulated Amortization**	**Net Amount**	**Gross Carrying Amount**	**Accumulated Amortization**	**Net Amount**
Developed technology	5 - 6	$ 48,556	$ (15,096)	$ 33,460	$ 43,455	$ (9,161)	$ 34,294
Backlog	1.25	10,500	(10,500)		10,500	(8,867)	1,633
Distributor license	1.5 - 2.5	2,052	(1,410)	642	1,860	(768)	1,092
In-process research and development (CPAC)	Indefinite				12,800		12,800
		$ 61,108	$ (27,006)	$ 34,102	$ 68,615	$ (18,796)	$ 49,819

Prior to the deconsolidation of CPAC on December 21, 2012 (see Note 9, Investment in CPAC), the Company had noted certain impairment triggers based on results of research and development work carried out by CPAC. As a result, based on projected future usage of the in-process research and development (IPR&D) technology by CPAC, an impairment charge of $12.2 million was recorded during the three months ended September 30, 2012. The Company did not identify any impairment triggers on goodwill or any of its other definite-lived intangible and long-lived assets.

Amortization expense related to intangible assets for the three and nine months ended March 31, 2013 was $2.2 million and $8.2 million, respectively. Amortization expense related to intangible assets for the three and nine months ended March 31, 2012 was $4.0 million and $12.2 million, respectively.

The estimated future amortization expense of purchased intangible assets as of March 31, 2013 is as follows (in thousands):

Year Ending June 30,	**Amount**
2013 (remaining 3 months)	$ 2,203
2014	8,382
2015	7,953
2016	7,953
2017	7,568
Thereafter	43
	$ 34,102

4. Financial Instruments

The following tables summarize the fair value of financial instruments measured on a recurring basis as of March 31, 2013 and June 30, 2012 (in thousands):

	Fair value measurement using			
Type of instrument and line item in condensed consolidated balance sheets	**Quoted Prices in Active Markets for Identical Instruments (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Total balance**
Assets at March 31, 2013				
Money market funds - included in cash and cash equivalents	$	$	$	$
Certificate of deposits - included in cash and cash equivalents	$ 5,038	$	$	$ 5,038
Assets at June 30, 2012				
Money market funds - included in cash and cash equivalents	$ 40,068	$	$	$ 40,068
Certificate of deposits - included in cash and cash equivalents	$ 6,742	$	$	$ 6,742

Table of Contents

The following tables summarize the fair value of financial instruments that are not measured on a recurring basis as of March 31, 2013 and June 30, 2012 (in thousands):

	Fair value measurement using			
Type of instrument and line item in condensed consolidated balance sheets	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total balance
At March 31, 2013				
3.75% Convertible Notes - included in long term debt	$	$ 89,200	$	$ 89,200
3.50% Convertible Notes - included in long term debt	$	$ 123,200	$	$ 123,200
At June 30, 2012				
3.75% Convertible Notes - included in long term debt	$	$ 101,400	$	$ 101,400

Long-term debt is measured on a non-recurring basis using Level 2 inputs based upon observable inputs of the Company s underlying stock price and the time value of the conversion option, since observable quoted prices of the 3.75% Convertible Notes and the 3.50% Convertible Notes are not readily available.

5. Commitments and Contingencies

Commitments

The Company s contractual obligations were presented in the Annual Report on Form 10-K for the previous annual reporting period ended June 30, 2012. There have been no material changes outside of the ordinary course of business in those obligations during the three and nine months ended March 31, 2013, except for the issuance of the 3.50% Convertible Notes during February 2013. See Note 8, Debt for additional information about the 3.50% Convertible Notes. Future payments expected for the 3.75% Convertible Notes and the 3.50% Convertible Notes as of March 31, 2013 are as follows (in thousands):

Year Ending June 30,	Amount
2013 (remaining 3 months)	$ 1,944
2014	7,775
2015	7,775
2016	7,775
2017	104,338
2018	117,348
Thereafter	
	$ 246,955

These amounts represent principal and interest cash payments over the life of the debt obligations, including anticipated interest payments that are not recorded on the Company s condensed consolidated balance sheet. Any conversion, redemption or purchase of Convertible Notes would impact cash payments.

Litigation

From time to time, the Company is involved in legal proceedings arising in the ordinary course of its business. Currently, management believes the Company does not have any probable and estimable loss related to any current legal proceedings and claims that would individually or in the aggregate materially adversely affect its financial condition or operating results. In excess of amounts accrued, management believes that there is a reasonable possibility that losses may be incurred for current legal proceedings. Management currently estimates a range of loss between zero and $3 million in the aggregate for such legal proceedings, where it is possible to make such estimates. Litigation is inherently unpredictable and is subject to significant uncertainties, some of which are beyond the Company s control. Should any of these estimates and assumptions change or prove to have been incorrect, the Company could incur significant charges related to legal matters which could have a material impact on its results of operations, financial position and cash flows.

Best Medical Trade Secret Litigation

On September 3, 2009, Best Medical International, Inc. (Best Medical) filed a lawsuit against the Company in the U.S. District Court for the Western District of Pennsylvania, claiming that the Company induced certain individuals to leave the employment of Best Medical and join the Company in order to gain access to Best Medical s confidential information and trade secrets. Best Medical is seeking monetary damages and other relief. The Company filed a motion for summary judgment on May 20, 2011, Best Medical filed its response on June 21, 2011, and the Company filed a response to their response on July 8, 2011. On October 25, 2011, the court granted summary judgment in favor of the Company on all counts. On November 21, 2011 Best Medical filed a notice of appeal, and the parties await a ruling by the appellate court.

Best Medical Patent Litigation

On August 6, 2010, Best Medical filed an additional lawsuit against the Company in the U.S. District Court for the Western District of Pennsylvania, claiming that the Company has infringed U.S. Patent No. 5,596,619, a patent that Best Medical alleges protects a method and apparatus for conformal radiation therapy. In December 2010 Best Medical amended its complaint by claiming that the Company also infringed U.S. Patent Nos. 6,038,283 and 7,266,175, both of which Best Medical alleges cover methods and apparatus for conformal radiation therapy. In March 2011, the Court dismissed with prejudice all counts against the Company, except for two counts of alleged willful infringement of two of the patents. Following several procedural rulings by the court, Best Medical moved to voluntarily dismiss one of the two remaining patent claims on June 28, 2011, which the court granted on June 30, 2011, leaving only one patent (U.S. Patent No. 6,038,283) at issue in the case. A mandatory mediation hearing was held in March 2013 during which the parties failed to reach settlement and another mediation hearing is scheduled for May 2013. If the parties fail to reach settlement then, we will continue to litigate this case. Best Medical is seeking declaratory and injunctive relief, as well as unspecified compensatory and treble damages and other relief.

Rotary Systems

On April 28, 2011, a former supplier to TomoTherapy, Rotary Systems Incorporated, filed suit in Minnesota state court, Tenth Judicial District, Anoka County, against TomoTherapy alleging misappropriation of trade secrets, as well as several other counts alleging various theories of injury. Rotary Systems alleges TomoTherapy misappropriated Rotary Systems trade secrets pertaining to a component previously purchased from Rotary Systems, which component TomoTherapy now purchases from a different supplier. The suit alleges TomoTherapy improperly supplied the alleged trade secrets to its present supplier, Dynamic Sealing Technologies Inc. (also a named defendant in the suit). Rotary Systems has made an unspecified claim for damages of greater than $50,000. TomoTherapy moved to dismiss the case on May 19, 2011, and on August 29, 2011, the court granted the motion to dismiss with respect to all counts other than the count alleging misappropriation of trade secrets. On May 21, 2012, the court granted the Company s motion for sanctions, in part, and gave Rotary Systems sixty days to identify the alleged trade secrets with specificity or face dismissal of its claim with prejudice. The court held a hearing on September 20, 2012 to review Rotary System s amended complaint and set a calendar for discovery. The court ruled on the amended complaint, and the parties have started discovery, which is expected to be completed by October 2013.

Radiation Stabilization Solutions Patent Litigation

On September 15, 2011, Radiation Stabilization Solutions LLC (RSS) filed a patent infringement complaint in the United States District Court for the Northern District of Illinois, Eastern Division. The complaint, alleged the Company s sale of the TomoHD product induces infringement of or contributorily infringes U.S. Patent No. 6,118,848, or the 848 Patent, and sought unspecified monetary damages for the alleged infringement. The complaint also named Varian Medical Systems, Inc., BrainLab AG, BrainLab, Inc., Elekta AB and Elekta, Inc. as defendants, alleging that certain of their products also infringe the 848 patent. On October 27, 2011, the Court dismissed the complaint without prejudice because non-resident defendants had been improperly named in the complaint.

On October 28, 2011, RSS filed a new complaint against the Company and a customer of the Company in the United States District Court for the Northern District of Illinois, Eastern Division. The new complaint repeats the original complaint s allegations against the Company and seeks unspecified monetary damages for the alleged infringement. The complaint further alleges that the customer directly and indirectly infringes the 848 patent, and seeks unspecified monetary damages for the alleged infringement. RSS also filed individual suits against each of Varian and Elekta and several of their respective customers. RSS served the complaint on Accuray and its customer on December 7, 2011. On January 30, 2012 the Company filed a motion to dismiss the complaint, and the Court heard oral argument for the motion on June 29, 2012. On August 21, 2012, the court granted the Company s motion in part and gave RSS leave to amend the complaint. On September 21, 2012, RSS filed an amended complaint. On November 2, 2012, the Company and RSS entered into a settlement agreement, under which the Company paid $150,000 to resolve all outstanding claims.

Accuray Securities Complaint

On November 1, 2012, a complaint was filed in Santa Clara County Superior Court purportedly on behalf of a class of shareholders seeking to enjoin the shareholder vote to be held at our annual meeting scheduled for November 30, 2012. The complaint named as defendants the Company and the members of the board of directors and alleged that the disclosures in the proxy statement for the annual meeting concerning the advisory vote on executive compensation and the proposal to amend the certificate of incorporation to increase the number of authorized shares are inadequate and constitute a breach of fiduciary duty. In addition to an injunction, the complaint sought unspecified monetary damages and other relief. The annual meeting was held on November 30, 2012. On December 28, 2012, the plaintiffs requested dismissal of the case from the court without prejudice, which was granted on January 3, 2013.

Table of Contents

Sarif Biomedical Patent Litigation

On January 28, 2013, Sarif Biomedical filed a patent infringement complaint against the Company in the United States District Court for Delaware. The complaint alleges the Company s CyberKnife System directly infringes U.S. Patent No. 5,755,725 and seeks unspecified monetary damages for the alleged infringement.

Software License Indemnity

Under the terms of the Company s software license agreements with its customers, the Company agrees that in the event the software sold infringes upon any patent, copyright, trademark, or any other proprietary right of a third party, it will indemnify its customer licensees against any loss, expense, or liability from any damages that may be awarded against its customer. The Company includes this infringement indemnification in all of its software license agreements and selected managed services arrangements. In the event the customer cannot use the software or service due to infringement and the Company cannot obtain the right to use, replace or modify the license or service in a commercially feasible manner so that it no longer infringes, then the Company may terminate the license and provide the customer a refund of the fees paid by the customer for the infringing license or service. The Company has not recorded any liability associated with this indemnification, as it is not aware of any pending or threatened actions that represent probable losses as of March 31, 2013.

6. Acquisition

On July 16, 2012, the Company acquired the remaining 90% of the outstanding shares of Morphormics, Inc. (Morphormics), a privately-held developer of medical imaging software based in North Carolina. The purpose of this acquisition was to enable the Company to extend auto-contouring capabilities for both the CyberKnife and TomoTherapy systems to improve disease specific workflows. The Company previously held 10% of the outstanding shares of Morphormics which was carried at zero value prior to the acquisition and re-measured to its acquisition-date fair value of $0.7 million based on the fair value of the consideration transferred. The acquisition has been accounted for as a business combination using purchase accounting and Morphormics results of operations are included in the condensed consolidated financial statements from July 16, 2012. The acquisition was not considered a material business combination and was funded through cash on-hand. In accordance with the terms of the acquisition agreement, $0.9 million of the purchase consideration was paid on April 16, 2013 and was included in other accrued liabilities in the condensed consolidated balance sheet at March 31, 2013. The Company has not incurred material severance or acquisition-related costs.

The fair value of total purchase consideration paid and payable for 100% of Morphormics equity interest as of the acquisition date was as follows (in thousands):

Cash paid and payable	$	5,385
Fair value of pre-existing investment in Morphormics		662
Total	$	6,047

The total purchase price was allocated to the net tangible and intangible assets acquired and liabilities assumed based on their fair values as of the acquisition date as follows (in thousands):

Cash and cash equivalents	$	668
Accounts receivable		283
Other current assets		7
Amortizable intangible assets - developed technology		5,100
Goodwill		77
Accrued compensation		(88)
Total purchase price	$	6,047

Pro forma results of operations for the acquisition have not been presented because they are not material to the Company s condensed consolidated statements of operations and comprehensive loss, balance sheets, or cash flows.

Table of Contents

7. Share-Based Compensation

The following table summarizes the share-based compensation charges included in the Company s condensed consolidated statements of operations and comprehensive loss (in thousands):

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2013	2012	2013	2012
Cost of revenue	$ 477	$ 276	$ 1,043	$ 1,271
Selling and marketing	256	165	803	545
Research and development	462	504	1,455	1,673
General and administrative	873	800	2,818	2,812
	$ 2,068	$ 1,745	$ 6,119	$ 6,301

At March 31, 2013 and June 30, 2012, capitalized share-based compensation expenses of $0.6 million and $0.4 million, respectively, were included as a component of inventories.

Performance-Based Awards (PSUs)

During fiscal 2012, the Compensation Committee of the Board of Directors of the Company approved the granting of PSUs to employees of the Company which vest only upon meeting certain financial performance criteria during the performance period commencing on the first day of the Company s 2012 fiscal year and ending on the last day of the Company s 2013 fiscal year. If the PSUs do not become vested as a result of the Company s performance during the performance period, all PSUs are automatically forfeited by the participants effective as of the last day of the performance period. During fiscal 2012, approximately 1.0 million PSUs were granted to employees valued at approximately $3.9 million which was based on the fair value of the Company s common stock on the grant date and will be recognized over the requisite performance period based on management s assessment of the probability of achieving the performance criteria. Approximately 0.6 million PSUs are outstanding as of March 31, 2013.

As of March 31, 2013, management assessed that it was not probable that the performance criteria would be met during the performance period and accordingly, no compensation cost has been recognized for the PSUs to date or during the three months ended March 31, 2013. If in a future period management revises its assessment and concludes that it is probable that the performance criteria will be met, the Company will record a cumulative catch-up compensation charge for the PSUs in that period. Remaining compensation charges would be recognized ratably over the remaining performance period.

Market Stock Unit (MSU) program

In October 2012, the Compensation Committee approved a new performance equity program, referred to as the market stock unit program (MSU Program). The MSU Program uses the Russell 2000 index as a performance benchmark and requires that the Company s total stockholder return exceed that of the Russell 2000. Based on a sliding scale of how much the Russell 2000 benchmark is exceeded, participating executives can earn up to a maximum of 150% of the target number of shares over two measurement periods, one at the end of fiscal 2014 and another at the end of fiscal 2015. During the nine months ended March 31, 2013, 0.4 million MSUs were granted to participating executives. The MSUs were valued at approximately $1.5 million based on a Monte-Carlo simulation on the grant date and will be recognized over a weighted average period of 1.8 years.

8. Debt

3.75% Convertible Senior Notes due August 2016

On August 1, 2011, the Company issued the 3.75% Convertible Notes to certain qualified institutional buyers or QIBs. The 3.75% Convertible Notes were offered and sold to the QIBs pursuant to Rule 144A under the Securities Act of 1933, as amended. The net proceeds from the $100 million offering, after deducting the initial purchaser s discount and commission and the related offering costs, were approximately $96.1 million. The offering costs and the initial purchaser s discount and commission (which are recorded in Other Assets) are both being amortized to interest expense using the effective interest method over five years. The 3.75% Convertible Notes bear interest at a rate of 3.75% per year, payable semi-annually in arrears in cash on February 1 and August 1 of each year, beginning on February 1, 2012. The 3.75% Convertible Notes will mature on August 1, 2016, unless earlier repurchased, redeemed or converted.

The 3.75% Convertible Notes were issued under an Indenture between the Company and The Bank of New York Mellon Trust Company, N.A., as trustee. Holders of the 3.75% Convertible Notes may convert their 3.75% Convertible Notes at any time on or after May 1, 2016 until the close of business on the business day immediately preceding the maturity date. Prior to May 1, 2016, holders of the 3.75% Convertible Notes may convert their 3.75% Convertible Notes only under the following circumstances: (1) during any calendar quarter after the calendar quarter ending September 30, 2011, and only during such calendar quarter, if the closing sale price of the Company s common stock for each of 20 or more trading days in the 30 consecutive trading days ending on the last trading day of the immediately preceding calendar quarter exceeds 130% of the conversion price in effect on the last trading day of the immediately preceding calendar quarter; (2) during the five consecutive business days immediately after any five consecutive trading-day period (such five consecutive trading-day period, the Note Measurement Period) in which the trading price per $1,000 principal amount of 3.75% Convertible Notes for each trading day of that Note Measurement Period was equal to or less than 98% of the product of the closing sale price of shares of the Company s common stock and the

Table of Contents

applicable conversion rate for such trading day; (3) if the Company calls any or all of the 3.75% Convertible Notes for redemption, at any time prior to the close of business on the business day immediately preceding the redemption date; or (4) upon the occurrence of specified corporate transactions as described in the Indenture. Upon conversion by holders of the 3.75% Convertible Notes, the Company will have the right to pay or deliver, as the case may be, cash, shares of common stock of the Company or a combination thereof, at the Company s election. At any time on or prior to the 33rd business day immediately preceding the maturity date, the Company may irrevocably elect to (a) deliver solely shares of common stock of the Company in respect of the Company s conversion obligation or (b) pay cash up to the aggregate principal amount of the 3.75% Convertible Notes to be converted and pay or deliver, as the case may be, cash, shares of common stock of the Company or a combination thereof in respect of the remainder, if any, of the Company s conversion obligation in excess of the aggregate principal amount of the 3.75% Convertible Notes being converted. The initial conversion rate is 105.5548 shares of the Company s common stock per $1,000 principal amount of 3.75% Convertible Notes (which represents an initial conversion price of approximately $9.47 per share of the Company s common stock). The conversion rate, and thus the conversion price, are subject to adjustment as further described below.

Holders of the 3.75% Convertible Notes who convert their 3.75% Convertible Notes in connection with a make-whole fundamental change, as defined in the Indenture, may be entitled to a make-whole premium in the form of an increase in the conversion rate. Additionally, in the event of a fundamental change, as defined in the Indenture, holders of the 3.75% Convertible Notes may require the Company to purchase all or a portion of their 3.75% Convertible Notes at a fundamental change repurchase price equal to 100% of the principal amount of 3.75% Convertible Notes, plus accrued and unpaid interest, if any, to, but not including, the fundamental change repurchase date.

On or after August 1, 2014 and prior to the maturity date, the Company may redeem for cash all or a portion of the 3.75% Convertible Notes if the closing sale price of its common stock exceeds 130% of the applicable conversion price (the initial conversion price is approximately $9.47 per share of common stock) of such 3.75% Convertible Notes for at least 20 trading days during any consecutive 30 trading-day period (including the last trading day of such period).

In accordance with Accounting Standards Codification (ASC) 470-20, *Debt with Conversion and Other Options*, the Company separately accounts for the liability and equity conversion components of the 3.75% Convertible Notes. The principal amount of the liability component of the 3.75% Convertible Notes was $75.9 million as of the date of issuance based on the present value of its cash flows using a discount rate of 10%, our approximate borrowing rate at the date of the issuance for a similar debt instrument without the conversion feature. The carrying value of the equity conversion component was $24.1 million. A portion of the initial purchaser s discount and commission and the offering costs totaling $0.9 million was allocated to the equity conversion component. The liability component will be accreted to the principal amount of the 3.75% Convertible Notes using the effective interest method over five years.

The following table presents the carrying value of the 3.75% Convertible Notes as of March 31, 2013 (in thousands):

Carrying amount of the equity conversion component	$	23,189
Principal amount of the 3.75% Convertible Notes	$	100,000
Unamortized debt discount (1)		(17,342)
Net carrying amount	$	82,658

(1)As of March 31, 2013, the remaining period over which the unamortized debt discount will be amortized is 40 months using an effective interest rate of 10.0%.

3.50% Convertible Senior Notes due February 2018

In February 2013, the Company issued $115 million aggregate principal amount of its 3.50% Convertible Notes to certain qualified institutional buyers or QIBs. The 3.50% Convertible Notes were offered and sold to the QIBs pursuant to Rule 144A under the Securities Act of 1933, as amended. The net proceeds from the offering, after deducting the initial purchaser s discount and commission and the related offering costs, were approximately $110.5 million. The offering costs and the initial purchaser s discount and commission (which are recorded in Other Assets) are both being amortized to interest expense using the effective interest method over five years. The 3.50% Convertible Notes bear interest at a rate of 3.50% per year, payable semi-annually in arrears in cash on February 1 and August 1 of each year, beginning on August 1, 2013. The 3.50% Convertible Notes will mature on February 1, 2018, unless earlier repurchased, redeemed or converted.

The 3.50% Convertible Notes were issued under an Indenture between the Company and The Bank of New York Mellon Trust Company, N.A., as trustee. Holders of the 3.50% Convertible Notes may convert their 3.50% Convertible Notes at any time until the close of business on the business day immediately preceding the maturity date. The 3.50% Convertible Notes are convertible, as described below into common stock of Accuray at an initial conversion rate equal to 187.6877 shares of common stock per $1,000 principal amount of the 3.50% Convertible Notes, which is equivalent to a conversion price of approximately $5.33 per share of common stock, subject to adjustment.

Holders of the 3.50% Convertible Notes who convert their 3.50% Convertible Notes in connection with a make-whole fundamental change , as defined in the Indenture, may be entitled to a make-whole premium in the form of an increase in the conversion rate. Additionally, in the event of a fundamental change, as defined in the Indenture, holders of the 3.50% Convertible

Table of Contents

Notes may require the Company to purchase all or a portion of their 3.50% Convertible Notes at a fundamental change repurchase price equal to 100% of the principal amount of 3.50% Convertible Notes, plus accrued and unpaid interest, if any, to, but not including, the fundamental change repurchase date.

In accordance with guidance in ASC 470-20, *Debt with Conversion and Other Options* and ASC 815-15, *Embedded Derivatives*, the Company determined that the embedded conversion components of the 3.50% Convertible Note do not require bifurcation and separate accounting. The $115 million principal amount of the 3.50% Convertible Note has been recorded in Long-term Debt on the condensed consolidated balance sheet as of March 31, 2013.

A summary of interest expenses on the 3.75% Convertible Note and the 3.50% Convertible Note for the three and nine months ended March 31, 2013 and 2012 were as follows (in thousands):

	Three months ended March 31,		Nine months ended March 31,	
	2013	**2012**	**2013**	**2012**
Interest expense related to contractual interest coupon	$ 1,441	$ 937	$ 3,316	$ 2,500
Interest expense related to amortization of debt discount	1,093	992	3,192	2,590
	$ 2,534	$ 1,929	$ 6,508	$ 5,090

9. Investment in CPAC

On December 21, 2012, the Company and CPAC entered into a Purchase Agreement and Release (the Purchase Agreement), whereby all the equity and debt investments held by the Company in CPAC were purchased by CPAC for a nominal consideration. Additionally, the Company assigned all its rights to the Dielectric Wall Accelerator (DWA) technology licensed from Lawrence Livermore National Security, LLC to CPAC. As a result of the Purchase Agreement, the Company has concluded that it is no longer the primary beneficiary of CPAC since it does not have any variable interests in that entity. Accordingly, the Company has deconsolidated CPAC and recorded a loss of $3.4 million during the three months ended December 31, 2012 due to the write-down of the carrying value of CPAC s net liabilities, the write-off of the receivables from CPAC and the non-controlling interest in CPAC, net of cash consideration received. The results of operations of CPAC, including the loss on deconsolidation of CPAC and the losses attributable to the non-controlling interest recorded during the three and nine months ended March 31, 2013 and 2012 have been disclosed as discontinued operations in the condensed consolidated statements of operations and comprehensive loss.

10. Restructuring Charges

During December 2012, the company vacated an office facility and recorded a charge of $1.4 million in general and administrative expenses during the three months ended December 31, 2012 for the remaining lease obligations on the facility, net of estimated sub-lease income. The company also recorded a change of $0.3 million in general and administrative expenses during the three months ended December 31, 2012 related to the disposition of certain fixed assets and leasehold improvements at this facility.

During the three months ended December 31, 2012, the company also recorded severance related charges of $2.2 million in general and administrative expenses due to the departure of Dr. Euan S.Thomson (former Chief Executive Officer), Mr. Chris Raanes (former Chief Operating Officer) and certain other employees.

On January 3, 2013, the Company announced a restructuring of operations to focus on improving commercial execution and position the Company to support sustainable revenue growth and profitability. The restructuring is expected to reduce staffing by approximately 13 percent and was heavily concentrated in the United States. During the three months ended March 31, 2013, the Company substantially completed the restructuring exercise, reduced its global workforce under this program by 108 full-time employees and recorded $4.9 million in charges for severance and related benefits for all affected employees. At March 31, 2013, approximately $2.0 million of the restructuring related liabilities were included in accrued compensation in the condensed consolidated balance sheet. The Company does not expect any significant severance-related charges to be incurred during the fourth quarter of fiscal 2013 and expects the remaining activities under this program to be substantially completed by the end of fiscal 2013. The Company expects annualized savings of approximately $17 million to $19 million of compensation related expenses as a result of this restructuring of operations. Restructuring charges are reflected within general and administrative expenses in the condensed consolidated statements of operations and comprehensive loss.

Table of Contents

Item 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis of our financial condition as of March 31, 2013 and results of operations for the three and nine months ended March 31, 2013 and 2012 should be read together with our condensed consolidated financial statements and related notes included elsewhere in this report. Statements made in this quarterly report on Form 10-Q that are not statements of historical fact are forward-looking statements and are subject to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Forward-looking statements in this report relate, but are not limited, to: expectations related to profitability and cash flows in fiscal 2013; sufficiency of cash resources and expected cash flows to fund future operations; expected uses of cash during fiscal 2013; the anticipated drivers of our future capital requirements; the impact of our prior sales reorganization on sales performance, particularly in the United States; the expected impact of and benefits from our recent restructuring of operations; anticipated increases in service revenue; the ongoing impact of purchase accounting adjustments; our expectations regarding the factors that will impact sales, competitive positioning and long-term success for our CyberKnife and TomoTherapy Systems; our expectations regarding the impact on our revenues and business of the introduction of our new CyberKnife and TomoTherapy Systems; the anticipated risks associated with our foreign operations and fluctuations in the U.S. dollar; the impact of recent legislation and regulation on our business; and the impact of the medical device excise tax on our business. Forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from expectations, including risks detailed from time to time under the heading Risk Factors in Part II, Item 1A of this report, Part I, Item 1A of the Company s annual report on Form 10-K for fiscal year 2012, Part II, Item 1A of the Company s quarterly reports on Form 10-Q for the quarters ended September 30, 2012 and December 31, 2012, respectively. Forward-looking statements speak only as of the date the statements are made and are based on information available to the Company at the time those statements are made and/or management s good faith belief as of that time with respect to future events. The Company assumes no obligation to update forward-looking statements to reflect actual performance or results, changes in assumptions or changes in other factors affecting forward-looking information, except to the extent required by applicable securities laws. Accordingly, investors should not place undue reliance on any forward-looking statements.

In this report, Accuray, the Company, we, us, and our refer to Accuray Incorporated and its subsidiaries.

Overview

Products and Markets

We believe we are a leading radiation oncology company with a history of rapid innovations. Our leading edge technologies are designed specifically to deliver radiosurgery, stereotactic body radiation therapy, intensity modulated radiation therapy, image guided radiation therapy and adaptive radiation therapy that is tailored to the specific needs of each patient. Our suite of products includes the CyberKnife® Systems and the TomoTherapy® Systems. The systems are generally complementary offerings, serving generally separate patient populations treated by the same medical specialty.

The CyberKnife Systems are robotic systems designed to deliver radiosurgery treatments to cancer tumors anywhere in the body. They are the only dedicated, full body robotic radiosurgery systems on the market. Radiosurgery is an alternative to traditional surgery for tumors and is performed on an outpatient basis in one to five treatment sessions. It allows for the treatment of patients who otherwise would not be treated with radiation, who may not be good candidates for surgery, or who desire non-surgical treatments. The use of radiosurgery with CyberKnife Systems to treat tumors throughout the body has grown significantly in recent years, but currently represents only a small portion of the patients who develop tumors treatable with CyberKnife Systems. A determination of when it may or may not be appropriate to use a CyberKnife System for treatment is at the discretion of the treating physician and depends on the specific patient. However, given the CyberKnife Systems design to treat focal tumors, the CyberKnife Systems are generally not used to treat (1) very large tumors, which are considerably wider than the radiation beam that can be delivered by CyberKnife Systems, (2) diffuse wide-spread disease, as is often the case for late stage cancers, because they are not localized (though CyberKnife Systems might be used to treat a focal area of the disease) and (3) systemic disease, like leukemias and lymphomas, which are not localized to an organ, but rather involve cells throughout the body.

In October 2012, we formally introduced two new versions of our technology platforms: the CyberKnife M6 Series and the TomoTherapy H Series. We expect that these new platforms will drive future orders and revenue growth. However, due to an aggressive product development and launch plan as well as certain manufacturing and supply issues affecting the new CyberKnife M6 Series with the Multileaf Collimator, or MLC, including low manufacturing yields with the MLC, we have experienced, and may continue to experience, delays in new orders and sales of these systems, which has had and may continue to have an adverse impact on our revenue levels and our business. Further continuation of these manufacturing and supply issues or the occurrence of new manufacturing and supply issues with either the CyberKnife M6 Series or the TomoTherapy H Series may adversely affect market acceptance of these new systems and negatively impact our revenue and our overall business.

Table of Contents

We believe that the long term success of the CyberKnife System is dependent on a number of factors including the following:

- Adoption of our recently introduced new CyberKnife platform and receipt of regulatory clearances associated with such new platform;
- Change in medical practice to utilize radiosurgery more regularly as an alternative to surgery or other treatments;
- Greater awareness among doctors and patients of the benefits of radiosurgery with the CyberKnife Systems;
- Continued evolution in clinical studies demonstrating the safety, efficacy and other benefits of using the CyberKnife Systems to treat tumors in various parts of the body;
- Continued advances in technology that improve the quality of treatments and ease of use of the CyberKnife Systems;
- Improved access to radiosurgery with the CyberKnife Systems in various countries through regulatory approvals;
- Medical insurance reimbursement policies that cover CyberKnife System treatments; and
- Expansion of sales of CyberKnife Systems in countries throughout the world.

The TomoTherapy Systems are advanced, fully integrated and versatile radiation therapy systems for the treatment of a wide range of cancer types. We began selling TomoTherapy Systems after our acquisition of TomoTherapy Incorporated on June 10, 2011. Radiation therapy is used in a variety of ways, often to treat tissue surrounding a tumor area after surgical removal of the tumor and also as the primary treatment for tumors. Radiation therapy treatments impact both cancer cells as well as healthy tissue; therefore the total prescribed radiation dose is divided into many fractions and delivered in an average of 25 to 35 treatment sessions over several weeks. Radiation therapy has been widely available and used in developed countries for decades, though many developing countries do not currently have a sufficient number of radiation therapy systems to adequately treat their domestic cancer patient populations. The number of radiation therapy systems in use and sold each year is currently many times larger than the number of radiosurgery systems. Large companies, including Varian Medical Systems, Inc. and Elekta AB, generate most of the sales in this market. We believe the TomoTherapy Systems offer clinicians and patients significant benefits over other radiation therapy systems in the market. We believe our ability to capture more sales in this established market will be influenced by a number of factors including the following:

- Adoption of our recently introduced new TomoTherapy platform and receipt of regulatory clearances associated with such new platform;

- Greater awareness among doctors and patients of the benefits of radiation therapy using TomoTherapy Systems;

- Advances in technology which improve the quality of treatments and ease of use of TomoTherapy Systems;

- Greater awareness among doctors of the improvement in reliability of TomoTherapy Systems; and

- Expansion of TomoTherapy System sales in countries throughout the world.

Sale of Our Products

Generating revenue from the sale of our systems is a lengthy process. Selling our systems, from first contact with a potential customer to a signed sales contract that meets our backlog criteria, generally spans six months to two years. The time from receipt of a signed contract to revenue recognition is governed generally by the time required by the customer to build, renovate or prepare the treatment room for installation of the system. This time varies significantly, generally from six to twenty-four months.

In the United States, we market to customers, including hospitals and stand-alone treatment facilities, directly through our sales organization. Outside the United States, we market to customers in over 92 countries directly and through distributors. We have sales and service offices in Japan and many countries in Europe and Asia.

The following table shows the number of systems installed by geographic region as of March 31, 2013:

	CyberKnife	TomoTherapy	Total
Americas	158	217	375
Europe, Middle East, India and Africa	64	100	164
Asia (excluding Japan)	36	60	96
Japan	25	33	58
Total	283	410	693

Table of Contents

International sales of our products account for a significant and growing portion of our total net revenue. Revenue derived from sales outside of the United States was approximately $42.2 million and $55.2 million for the three months ended March 31, 2013 and 2012, respectively, and represented 60% and 54% of our net sales during these periods, respectively. Revenue derived from sales outside of the United States was approximately $131.8 million and $158.9 million for the nine months ended March 31, 2013 and 2012, respectively, and represented 57% and 51% of our net sales during these periods, respectively.

Backlog

We report backlog in the following manner:

- Products: Orders for systems, upgrades, and our shared ownership program are reported in backlog, excluding amounts attributable to PCS (warranty period services and post warranty services), installation, training and professional services.

- Service: Orders for PCS, installation services, training and professional services are not reported in backlog.

For orders that cover both products and services, only the portion of the order that is recognized as product revenue is reported as backlog. The portion of the order that is recognized as service revenue (for example, PCS) is not included in reported backlog. Additionally, orders for TomoTherapy Systems made on or before June 30, 2011, that met the historical TomoTherapy backlog criteria have been grandfathered into, and are included in, our backlog, with the exception of orders that would have aged out as of June 30, 2011. TomoTherapy previously did not have an age out criteria, so we have adjusted the TomoTherapy backlog to age out orders where 2.5 years have passed from the time the order entered TomoTherapy s backlog. As of March 31, 2013, product only backlog was $297.9 million as compared to $279.6 million as of March 31, 2012.

In order for the product portion of a sales agreement to be counted as backlog, it must meet the following criteria:

- The contract is signed and properly executed by both the customer and us. A customer purchase order that is signed and incorporates the terms of our contract quote will be considered equivalent to a signed and executed contract;

- The contract is non-contingent it either has cleared all its contingencies or contains no contingencies when signed;

- We have received a minimum deposit or a letter of credit; the sale is a direct channel sale to a government entity, or the product has shipped to a customer with credit sufficient to cover the minimum deposit;

- The specific end customer site has been identified by the customer in the written contract or written amendment; and

- Less than 2.5 years have passed since the contract met all the criteria above.

Although our backlog includes only contractual agreements from our customers to purchase CyberKnife Systems or TomoTherapy Systems, we cannot provide assurance that we will convert backlog into recognized revenue due to factors outside our control, which includes, without limitation, changes in customers needs or financial condition, changes in government or health insurance reimbursement policies, changes to regulatory requirements, or other reasons for cancellation of orders.

We also use book-to-bill ratios to assess the quality and growth of our backlog. The ratio is calculated for a period as new orders booked and included in backlog upon meeting criteria described above less any orders cancelled from backlog, and the resultant net orders being divided by total product revenue recognized during that period.

Table of Contents

Results of Continuing Operations

Three and nine month periods ended March 31, 2013 compared to three and nine month periods ended March 31, 2012

Net Revenue

(Dollars in thousands)	Three Months Ended March 31, 2013	Three Months Ended March 31, 2012	Variance	Variance in Percent	Nine Months Ended March 31, 2013	Nine Months Ended March 31, 2012	Variance	Variance in Percent
Products	$ 25,023	$ 59,875	$ (34,852)	-58%	$ 98,821	$ 179,851	$ (81,030)	-45%
Services	45,524	41,720	3,804	9%	132,253	127,218	5,035	4%
Other		221	(221)	-100%		1,621	(1,621)	-100%
Net Revenue	$ 70,547	$ 101,816	$ (31,269)	-31%	$ 231,074	$ 308,690	$ (77,616)	-25%

Total revenues during the three months ended March 31, 2013 decreased by 31% from the three months ended March 31, 2012 primarily due to lower product revenues. We recognized revenues on 9 units during the three months ended March 31, 2013 as compared to 21 units during the three months ended March 31, 2012. The decrease in units along with a decline in average selling price per unit resulted in decreases in product revenues of $34.9 million during the three months ended March 31, 2013 as compared to the three months ended March 31, 2012.

Total revenues during the nine months ended March 31, 2013 decreased by 25% from the nine months ended March 31, 2012 primarily due to lower product revenues. We recognized revenues on 36 units during the nine months ended March 31, 2013 as compared to 69 units during the nine months ended March 31, 2012. This resulted in decreases in product revenues of $81.0 million during the nine months ended March 31, 2013 as compared to the nine months ended March 31, 2012. During the three and nine months ended March 31, 2013, product revenues from the sale of our units have continued to be slow primarily in the North American and Asia-Pacific regions due to the slowdown in capital expenditures by hospitals, continued uncertainties around economic growth in certain key markets, and the lack of availability of the new models of the CyberKnife System and the TomoTherapy System.

Services revenues during the three and nine months ended March 31, 2013 increased by $3.8 million and $5.0 million, respectively, from the three and nine months ended March 31, 2012. Service revenues during the three and nine months ended March 31, 2012 included $1.9 million and $10.6 million, respectively, of service revenues arising from purchase accounting adjustments related to the TomoTherapy acquisition which was completed in June 2011. Such purchase accounting adjustments were not material during the three and nine months ended March 31, 2013. Excluding such adjustments, service revenues increased by $5.7 million and $15.6 million, respectively, during the three and nine months ended March 31, 2013 as compared to the three and nine months ended March 31, 2012 primarily due to increases in sales of higher priced maintenance contracts, particularly to customers using the TomoTherapy systems, as well as an increase in our installed base. We expect our service revenue to increase as our installed base continues to grow.

Gross Profit

(Dollars in thousands)	Three Months Ended March 31, 2013 (Dollars in thousands)	2013 (% of net revenue)	2012 (Dollars in thousands)	2012 (% of net revenue)	Nine Months Ended March 31, 2013 (Dollars in thousands)	2013 (% of net revenue)	2012 (Dollars in thousands)	2012 (% of net revenue)
Gross profit	$ 20,053	28.4%	$ 36,111	35.5%	$ 70,355	30.4%	$ 100,782	32.6%
Products	6,620	26.5%	27,474	45.9%	37,845	38.3%	76,277	42.4%
Services	13,433	29.5%	8,620	20.7%	32,510	24.6%	23,592	18.5%
Other		0.0%	17	7.7%		0.0%	913	56.3%

The overall gross profit margin during the three and nine months ended March 31, 2013 declined by 7.1 percentage points and 2.2 percentage points, respectively, as compared to the three and nine months ended March 31, 2012. Product margins were lower during the three and nine months ended March 31, 2013 primarily due to higher cost of units sold attributed to higher per-unit production-related costs resulting from lower volume of production and lower revenues per unit, partially offset by the favorable impact of a net reduction in purchase accounting adjustments resulting from the acquisition of TomoTherapy on June 10, 2011. Service margins were higher during the three and nine months ended March 31, 2013 primarily due to improvements in the reliability of the TomoTherapy Systems leading to reduced parts usage and other cost saving initiatives, partially offset by the unfavorable impact of a net reduction in purchase accounting adjustments resulting from the acquisition of TomoTherapy on June 10, 2011.

In accordance with purchase accounting standards, a number of adjustments were recorded to the value of assets and liabilities of TomoTherapy as of the closing of the acquisition on June 10, 2011. These included the write-up of inventory based on selling price rather than cost of manufacturing, the write-down of deferred product revenue, the write-up of deferred service revenue, and the recording of intangible assets related to developed technology and to backlog existing at the time of the acquisition. On the acquisition date, deferred service and product revenues were valued at cost plus a reasonable margin. Purchase accounting adjustments decreased gross profits for the three months ended March 31, 2012 by $2.7 million as follows: Product revenues were reduced by $1.3 million while product cost of revenues was increased by $3.8 million; Services revenues were increased by $1.9 million while services cost of revenues was decreased by $0.5 million. Purchase

Table of Contents

accounting adjustments reduced gross profit for the nine months ended March 31, 2012 by $11.8 million as follows: Product revenues were reduced by $1.9 million, while product cost of revenues was increased by $19.7 million; Services revenues were increased by $10.6 million while services cost of revenues was increased by $0.8 million. Purchase accounting adjustments reduced gross profit for the three and nine months ended March 31, 2013 by $1.7 million and $6.9 million, respectively, resulting primarily from the increases in product cost of revenues by $1.7 million and $6.8 million, respectively.

Selling and Marketing

(Dollars in thousands)	Three Months Ended March 31, 2013	Three Months Ended March 31, 2012	Variance	Variance in Percent	Nine Months Ended March 31, 2013	Nine Months Ended March 31, 2012	Variance	Variance in Percent
Selling and marketing	$ 12,646	$ 12,449	$ 197	2%	$ 41,296	$ 40,047	$ 1,249	3%
Percentage of net revenue	*17.9%*	*12.2%*			*17.9%*	*13.0%*		

Selling and marketing expenses increased by $0.2 million during the three months ended March 31, 2013 as compared to the three months ended March 31, 2012 primarily due to higher compensation related costs of $0.8 million and travel related costs of $0.2 million, resulting from a re-organization of the marketing function, partially offset by cost control initiatives, resulting in lower facilities and information technology related expenses of $0.5 million and tradeshow and advertising related expenses of $0.3 million.

Selling and marketing expenses increased by $1.2 million during the nine months ended March 31, 2013 as compared to the nine months ended March 31, 2012 primarily due to higher tradeshow and advertising related expenses of $1.8 million and consulting expenses of $0.3 million related to the introduction of two new products at an industry trade show in October 2012, partially offset by lower travel related expenses of $0.5 million and other operational expenses of $0.2 million due to cost control initiatives.

Research and Development

(Dollars in thousands)	Three Months Ended March 31, 2013	Three Months Ended March 31, 2012	Variance	Variance in Percent	Nine Months Ended March 31, 2013	Nine Months Ended March 31, 2012	Variance	Variance in Percent
Research and development	$ 15,697	$ 22,398	$ (6,701)	-30%	$ 51,510	$ 59,799	$ (8,289)	-14%
Percentage of net revenue	*22.3%*	*22.0%*			*22.3%*	*19.4%*		

Research and development expenses decreased by $6.7 million during the three months ended March 31, 2013 as compared to the three months ended March 31, 2012 primarily due to decreases in consulting and project related costs of $3.4 million and facilities and information technology related costs of $1.8 million due to cost control initiatives and a reduction in development related activities after the two new product introductions at an industry trade show in October 2012 as well as lower compensation related costs of $0.9 million and travel related costs of $0.5 million resulting from a re-organization of the research and development function.

Research and development expenses decreased by $8.3 million during the nine months ended March 31, 2013 as compared to the nine months ended March 31, 2012 primarily due to decreases in consulting and project related costs of $5.3 million and facilities and information technology related costs of $1.7 million due to cost control initiatives and a reduction in development related activities after the two new product introductions at an industry trade show in October 2012 as well as lower compensation related costs of $0.7 million and travel related costs of $0.6 million resulting from a re-organization of the research and development function during the three months ended March 31, 2013.

General and Administrative

	Three Months Ended March 31,				Nine Months Ended March 31,			
(Dollars in thousands)	**2013**	**2012**	**Variance**	**Variance in Percent**	**2013**	**2012**	**Variance**	**Variance in Percent**
General and administrative	$ 16,745	$ 13,964	$ 2,781	20%	$ 45,479	$ 42,047	$ 3,432	8%
Percentage of net revenue	*23.7%*	*13.7%*			*19.7%*	*13.6%*		

General and administrative expenses increased by $2.8 million during the three months ended March 31, 2013 as compared to the three months ended March 31, 2012 primarily due to $4.9 million of severance charges incurred due to the restructuring of operations announced in January 2013. This was partially offset by lower compensation related costs of $1.1 million, lower consulting, legal and accounting related expenses of $0.6 million and lower travel and operational expenses of $0.4 million due to cost control initiatives.

General and administrative expenses increased by $3.4 million during the nine months ended March 31, 2013 as compared to the nine months ended March 31, 2012 primarily due to $7.2 million of severance charges incurred for the departure of our former CEO, COO and other employees in the three months ended December 31, 2012 and the restructuring of operations announced in January 2013 and $1.7 million related to lease acceleration and fixed asset disposal charges from vacating an office facility during December 2012. This was partially offset by lower consulting, legal and accounting related expenses of $2.8 million, lower compensation related costs of $2.1 million, lower facilities and information technology related costs of $0.3 million and lower travel and operational related expenses of $0.2 million due to cost control initiatives.

Table of Contents

Other Expense, Net

(Dollars in thousands)	Three Months Ended March 31, 2013	2012	Variance	Variance in Percent	Nine Months Ended March 31, 2013	2012	Variance	Variance in Percent
Other expense, net	$ (5,565)	$ (838)	$ (4,727)	564%	$ (8,849)	$ (8,074)	$ (775)	10%

Net other expense increased by $4.7 million during the three months ended March 31, 2013 as compared to the three months ended March 31, 2012. During the three months ended March 31, 2013, we recognized net other expense of $5.6 million primarily due to $2.8 million of interest expense related to our 3.75% Convertible Notes and 3.50% Convertible Notes and $2.5 million of foreign currency losses primarily resulting from the depreciation of the Japanese Yen against the U.S. Dollar. During the three months ended March 31, 2012, we recognized net other expense of $0.8 million primarily due to $2.0 million of interest expense related to our 3.75% Convertible Notes, partially offset by foreign currency gains of $1.2 million primarily due to the strengthening of the Euro and the Swiss Franc against the U.S. Dollar.

Net other expense increased by $0.8 million during the nine months ended March 31, 2013 as compared to the nine months ended March 31, 2012. During the nine months ended March 31, 2013, we recognized net other expense of $8.8 million primarily due to $7.0 million of interest expense related to our 3.75% Convertible Notes and 3.50% Convertible Notes and $2.2 million of foreign currency losses primarily resulting from the depreciation of the Japanese Yen against the U.S. Dollar, partially offset by a $0.7 million gain on our previously held equity interest in Morphormics, Inc., resulting from our acquisition of Morphormics on July 16, 2012. During the nine months ended March 31, 2012, we recognized net other expense of $8.1 million primarily due to $5.3 million of interest expense related to our 3.75% Convertible Notes, which were issued on August 1, 2011 and $2.6 million of foreign currency losses primarily resulting from the strengthening of the U.S. Dollar against the Euro and the Swiss Franc.

Provision for Incomes Taxes

(Dollars in thousands)	Three Months Ended March 31, 2013	2012	Variance	Variance in Percent	Nine Months Ended March 31, 2013	2012	Variance	Variance in Percent
Provision for income taxes	$ 603	$ 1,247	$ (644)	-52%	$ 1,867	$ 2,152	$ (285)	-13%
Percentage of loss before provision for income taxes	*-2.0%*	*-9.2%*			*-2.4%*	*-4.4%*		

On a quarterly basis, we provide for income taxes based upon an estimated annual effective income tax rate. Income tax expenses were $0.6 million and $1.9 million for the three and nine months ended March 31, 2013 respectively, compared to income tax expenses of $1.2 million and $2.2 million for the three and nine months ended March 31, 2012 respectively. The decrease in tax expenses were primarily related to the release of tax reserves in certain foreign subsidiaries due to the expiration of statutes of limitation and the completion of tax audits.

Restructuring Charges

During December 2012, we vacated an office facility and recorded a charge of $1.4 million in general and administrative expenses during the three months ended December 31, 2012 for the remaining lease obligations on the facility, net of estimated sub-lease income. We also recorded a charge of $0.3 million in general and administrative expenses during the three months ended December 31, 2012 related to the disposition of certain fixed assets and leasehold improvements at this facility.

During the three months ended December 31, 2012, we also recorded severance related charges of $2.2 million in general and administrative expenses due to the departure of Dr. Euan S. Thomson (former Chief Executive Officer), Mr. Chris Raanes (former Chief Operating Officer) and certain other