

Xtant Medical Holdings, Inc.
Form 10-Q
November 10, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark one)

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

For the quarterly period ended September 30, 2016

OR

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

For the transition period from to

Commission file number: 001-34951

XTANT MEDICAL HOLDINGS, INC.

(Exact name of registrant as specified in its charter)

Delaware 20-5313323
(State or other jurisdiction (I.R.S. Employer)

of incorporation or organization) Identification No.)

664 CRUISER LANE

BELGRADE, MONTANA 59714

(Address of principal executive offices) (Zip code)

(406) 388-0480

(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 No

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

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

Number of shares of common stock, \$0.000001 par value, of registrant outstanding at November 8, 2016: 12,193,970.

XTANT MEDICAL HOLDINGS, INC.

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PART I - FINANCIAL INFORMATION**ITEM 1. FINANCIAL STATEMENTS****XTANT MEDICAL HOLDINGS, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS**

	As of September 30, 2016 (unaudited)	As of December 31, 2015
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 1,408,608	\$ 6,368,016
Trade accounts receivable, net of allowance for doubtful accounts of \$2,997,747 and \$2,579,634, respectively	15,826,130	15,385,218
Current inventories, net	26,499,085	22,684,716
Prepaid and other current assets	2,034,127	601,697
Total current assets	45,767,950	45,039,647
Non-current inventories, net	1,271,425	1,607,915
Property and equipment, net	16,012,138	11,816,629
Goodwill	41,534,626	41,534,626
Intangible assets, net	37,021,472	40,237,289
Other assets	841,354	791,221
Total assets	\$ 142,448,965	\$ 141,027,327
LIABILITIES & STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 12,889,056	\$ 9,386,531
Accounts payable - related party (Note 15)	1,060,200	1,406,763
Revolving line of credit	8,353,117	-
Accrued liabilities	5,623,574	9,595,851
Warrant derivative liability	333,613	1,050,351
Current portion of capital lease obligations	209,826	35,139
Total current liabilities	28,469,386	21,474,635
Long-term liabilities:		
Capital lease obligation, less current portion	720,265	7,800

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Long-term convertible debt, less issuance costs	68,864,974	66,436,647
Long-term debt, less issuance costs	49,493,259	44,231,718
Total liabilities	147,547,884	132,150,800
Commitments and Contingencies (Note 12)		
Stockholders' (deficit) equity:		
Preferred stock, \$0.000001 par value; 5,000,000 shares authorized; no shares issued and outstanding	-	-
Common stock, \$0.000001 par value; 95,000,000 shares authorized; shares issued and outstanding as of September 30, 2016 12,193,970 and shares issued and outstanding as of December 31, 2015 11,897,601	11	11
Additional paid-in capital	82,898,754	81,917,488
Accumulated deficit	(87,997,684)	(73,040,972)
Total stockholders' (deficit) equity	(5,098,919)	8,876,527
Total liabilities & stockholders' (deficit) equity	\$ 142,448,965	\$ 141,027,327

See notes to unaudited condensed consolidated financial statements.

XTANT MEDICAL HOLDINGS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2016	2015	2016	2015
Revenue				
Orthopedic product sales	\$22,907,717	\$17,421,397	\$65,025,908	\$36,431,354
Other revenue	186,423	271,623	505,971	657,395
Total Revenue	23,094,140	17,693,020	65,531,879	37,088,749
Cost of sales	7,114,041	6,035,673	20,749,381	12,883,439
Gross Profit	15,980,099	11,657,347	44,782,498	24,205,310
Operating Expenses				
General and administrative	3,773,236	3,980,805	11,216,112	8,805,104
Sales and marketing	11,242,820	8,430,303	32,115,763	18,179,552
Research and development	928,930	794,464	2,612,402	1,519,196
Depreciation and amortization	1,265,490	1,541,220	3,690,519	1,765,994
Acquisition and integration related expenses (Note 2)	517,083	3,856,519	1,269,613	3,856,519
Extinguishment of debt	0	(2,345,019)	0	(2,345,019)
Impairment of assets	0	233,748	0	233,748
Non-cash consulting expense	156,129	50,000	266,721	190,869
Total Operating Expenses	17,883,688	16,542,040	51,171,130	32,205,963
Loss from Operations	(1,903,589)	(4,884,693)	(6,388,632)	(8,000,653)
Other Income (Expense)				
Interest expense	(3,163,534)	(2,111,721)	(8,974,895)	(4,930,941)
Change in warrant derivative liability	220,409	397,366	716,738	(78,923)
Non-cash consideration associated with stock purchase agreement	-	-	-	(558,185)
Other income (expense)	(51,350)	(89,926)	(309,924)	(193,052)
Total Other Income (Expense)	(2,994,475)	(1,804,281)	(8,568,081)	(5,761,101)
Net Loss from Operations	\$(4,898,064)	\$(6,688,974)	\$(14,956,713)	\$(13,761,754)
Net loss per share:				
Basic	\$(0.40)	\$(0.64)	\$(1.24)	\$(1.70)
Dilutive	\$(0.40)	\$(0.64)	\$(1.24)	\$(1.70)

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Shares used in the computation:

Basic	12,193,970	10,432,622	12,064,782	8,100,226
Dilutive	12,193,970	10,432,622	12,064,782	8,100,226

See notes to unaudited condensed consolidated financial statements.

XTANT MEDICAL HOLDINGS, INC.**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(Unaudited)

	Nine Months Ended September 30,	
	2016	2015
Operating activities:		
Net loss	\$(14,956,713)	\$(13,761,754)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	5,551,854	2,403,934
Non-cash interest	4,477,148	1,665,172
Extinguishment of debt	-	(2,345,019)
Non-cash consideration associated with stock purchase agreement	-	558,185
Impairment of assets	-	233,748
Amortization of debt discount	-	707,281
(Gain) Loss on sale of fixed assets	(14,149)	11,377
Non-cash consulting expense/stock option expense	522,987	881,681
Provision for losses on accounts receivable and inventory	898,285	805,684
Change in derivative warrant liability	(716,738)	78,923
Changes in operating assets and liabilities:		
Accounts receivable	(859,026)	(2,801,124)
Inventories	(3,958,050)	477,818
Prepaid and other assets	(1,482,561)	(325,976)
Accounts payable	3,155,962	694,326
Accrued liabilities	(3,813,998)	1,688,664
Net cash used in operating activities	(11,194,999)	(9,027,080)
Investing activities:		
Acquisition of X-spine Systems, Inc.	-	(73,033,049)
Purchases of property and equipment and intangible assets	(5,566,569)	(444,312)
Proceeds from sale of fixed assets	16,400	102,587
Net cash used in investing activities	(5,550,169)	(73,374,774)
Financing activities:		
Payments on long-term debt	-	(38,668)
Net proceeds from equity private placement	-	515,395
Payment on royalty obligation	-	(542,905)
Proceeds from the issuance of capital leases	-	70,921
Payments on capital leases	(80,071)	(78,490)
Net proceeds from the issuance of long-term debt	1,000,000	17,479,159
Net proceeds from the issuance of convertible debt	2,212,718	66,322,366
Net proceeds from the revolving line of credit	8,353,113	-

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Net proceeds from issuance of stock	300,000	2,118,483
Net cash provided by financing activities	11,785,760	85,846,261
Net change in cash and cash equivalents	(4,959,408)	3,444,407
Cash and cash equivalents at beginning of period	6,368,016	4,526,026
Cash and cash equivalents at end of period	\$ 1,408,608	\$ 7,970,433

See notes to unaudited condensed consolidated financial statements.

Notes to Unaudited Condensed Consolidated Financial Statements

(1) Business Description and Summary of Significant Accounting Policies

Business Description

The accompanying condensed consolidated financial statements include the accounts of Xtant Medical Holdings, Inc. (“Xtant”), formerly known as Bacterin International Holdings, Inc., a Delaware corporation, and its wholly owned subsidiaries, Bacterin International, Inc., (“Bacterin”) a Nevada corporation, Xtant Medical, Inc. (“Xtant Medical”), a Delaware corporation, and X-spine Systems, Inc. (“X-spine”), an Ohio corporation, (Xtant, Xtant Medical, Bacterin and X-spine are jointly referred to herein as the “Company”). All intercompany balances and transactions have been eliminated in consolidation. Xtant develops, manufactures and markets orthopedic products for domestic and international markets. Xtant products serve the combined specialized needs of orthopedic and neurological surgeons, including orthobiologics for the promotion of bone healing, implants and instrumentation for the treatment of spinal disease, tissue grafts for the treatment of orthopedic disorders to promote healing following spine, cranial and surgeries and the development, manufacturing and sale of medical devices for use in orthopedic spinal surgeries. The Company also previously developed and licensed coatings for various medical device applications.

On July 31, 2015, Xtant acquired all of the outstanding capital stock of X-spine Systems, Inc. for approximately \$60 million in cash, repayment of approximately \$13 million of X-spine debt, and approximately 4.24 million shares of Xtant common stock (See Note 2, “Business Combination” below). Following the closing of the acquisition, on July 31, 2015, Bacterin International Holdings, Inc. changed its name to Xtant Medical Holdings, Inc. On August 6, 2015, Xtant formed a new wholly owned subsidiary, Xtant Medical, to facilitate the integration of Bacterin and X-spine.

The markets in which the Company competes are highly competitive and rapidly changing. Significant technological advances, changes in customer requirements, or the emergence of competitive products with new capabilities or technologies could adversely affect the Company’s operating results. The Company’s business could be harmed by a decline in demand for, or in the prices of, its products or as a result of, among other factors, any change in pricing or distribution methods, increased price competition, changes in government regulations or a failure by the Company to keep up with technological change. Further, a decline in available donors could have an adverse impact on our business.

The accompanying interim condensed consolidated financial statements of Xtant for the three and nine months ended September 30, 2016 and 2015 are unaudited and are prepared in accordance with accounting principles generally accepted in the United States of America. They do not include all disclosures required by generally accepted accounting principles for annual financial statements, but in the opinion of management, include all adjustments,

consisting only of normal recurring items, necessary for a fair presentation. Interim results are not necessarily indicative of results which may be achieved in the future for the full year ending December 31, 2016.

These financial statements should be read in conjunction with the financial statements and notes thereto which are included in Xtant's Annual Report on Form 10-K for the year ended December 31, 2015. The accounting policies set forth in those annual financial statements are the same as the accounting policies utilized in the preparation of these financial statements, except as modified for appropriate interim financial statement presentation.

Concentrations and Credit Risk

The Company’s accounts receivable are due from a variety of health care organizations and distributors throughout the world. Approximately 95% of sales were in the United States for the nine months ended September 30, 2016 and 2015. No single customer accounted for more than 10% of revenue or accounts receivable for the comparable periods. The Company provides for uncollectible amounts when specific credit issues arise. Management’s estimates for uncollectible amounts have been adequate during prior periods, and management believes that all significant credit risks have been identified at September 30, 2016.

In the nine months ended September 30, 2016, Xtant purchased from Norwood Medical approximately 12% of its operating products (See Note 15, “Related Party Transactions” below).

Revenue by geographical region is as follows:

	Nine Months Ended September 30,	
	2016	2015
United States	\$62,253,220	\$35,419,434
Rest of world	3,278,659	1,669,315
Total revenue	\$65,531,879	\$37,088,749

Use of Estimates

The preparation of the financial statements requires management of the Company to make a number of estimates and assumptions relating to the reported amount of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the period. Significant estimates include the carrying amount of property and equipment, goodwill, and intangible assets and liabilities; valuation allowances for trade receivables, inventory, and deferred income tax assets and liabilities; valuation of the warrant derivative liability, inventory and estimates for the fair value of stock options grants and other equity awards upon which the Company determines stock-based compensation expense. Actual results could differ from those estimates.

Long-Lived Assets

Long-lived assets, including intangible assets, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the estimated fair value of the assets. (See Note 5, "Impairment of Assets" below.)

Goodwill

Goodwill represents the excess of costs over fair value of assets of businesses acquired. Goodwill and intangible assets acquired in a purchase business combination and determined to have indefinite useful lives are not amortized, instead they are tested for impairment at least annually and whenever events or circumstances indicate the carrying amount of such asset may not be recoverable. In its evaluation of goodwill, the Company performs an assessment of qualitative factors to determine if it is more-likely-than-not that goodwill might be impaired and whether it is necessary to perform the two-step goodwill impairment. The Company conducts its annual impairment test on December 31 of each year.

Revenue Recognition

Revenue is recognized when all of the following criteria are met: a) the Company has entered into a legally binding agreement with the customer; b) the products or services have been delivered; c) the Company's fee for providing the products and services is fixed or determinable; and d) collection of the Company's fee is probable.

The Company's policy is to record revenue net of any applicable sales, use, or excise taxes. If an arrangement includes a right of acceptance or a right to cancel, revenue is recognized when acceptance is received or the right to cancel has expired.

The Company ships to certain customers under consignment arrangements whereby the Company's product is stored by the customer. The customer is required to report the use to the Company and upon such notice, the Company invoices the customer and revenue is recognized when above criteria have been met.

Advertising Costs

The Company expenses advertising costs as incurred. The Company had advertising expense of \$140,049 and \$93,854 for the nine months ended September 30, 2016 and 2015, respectively.

Research and Development

Research and development costs, which are principally related to internal costs for the development of new devices and biologics and processes are expensed as incurred.

Other Income (Expense)

Other income (expense) primarily consists of non-recurring items that are outside of the normal Company's operations such as other related legal expenses, gain or loss on the sale of fixed assets and miscellaneous minor adjustments to account balances.

Net Loss Per Share

Basic net income (loss) per share is computed by dividing net income (loss) by the weighted average number of common shares outstanding. Shares issued during the period and shares reacquired during the period are weighted for the portion of the period that they were outstanding. Diluted net income (loss) per share is computed in a manner consistent with that of basic earnings per share while giving effect to all potentially dilutive common shares outstanding during the period, which include the assumed exercise of stock options and warrants using the treasury stock method. Diluted net loss per share was the same as basic net loss per share for the three and nine months ended September 30, 2016 and 2015, as shares issuable upon the exercise of stock options and warrants were anti-dilutive as a result of the net losses incurred for those periods. Dilutive earnings per share are not reported as their effects of including 1,794,792 and 1,896,253 outstanding stock options and warrants for the three and nine months ended September 30, 2016 and 2015, respectively, are anti-dilutive.

Fair Value of Financial Instruments

The carrying values of financial instruments, including trade accounts receivable, accounts payable, other accrued expenses and long-term debt, approximate their fair values based on terms and related interest rates.

The Company follows a framework for measuring fair value. The framework provides a hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The three levels of the fair value hierarchy are described below:

Level 1: Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets.

Level 2: Inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

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A financial instrument's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. During the three and nine months ended September 30, 2016 and 2015, there was no reclassification in financial assets or liabilities between Level 1, 2 or 3 categories.

The following table sets forth by level, within the fair value hierarchy, our liabilities as of September 30, 2016 and December 31, 2015, that are measured at fair value on a recurring basis:

Warrant derivative liability

	As of September 30, 2016	As of December 31, 2015
Level 1	-	-
Level 2	-	-
Level 3	\$ 333,613	\$ 1,050,351

The valuation technique used to measure fair value of the warrant liability is based on a valuation model and significant assumptions and inputs determined by us (See Note 11, "Warrants" below).