

VITAL IMAGES INC
Form 10-Q
May 10, 2006

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2006

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 0-22229

VITAL IMAGES, INC.

(Exact name of registrant as specified in its charter)

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Minnesota
(State or other jurisdiction of
incorporation or organization)

42-1321776
(I.R.S. Employer Identification No.)

5850 Opus Parkway, Suite 300
Minnetonka, Minnesota
(Address of principal
executive offices)

55343-4414
(Zip Code)

(952) 487-9500

(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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

On May 5, 2006, there were 13,188,614 shares of the Registrant's common stock, par value \$.01 per share, outstanding.

Vital Images, Inc.

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March 31, 2006

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Part I. Financial Information

Item 1. Financial Statements

Vital Images, Inc. Condensed Consolidated Balance Sheets

(Unaudited)

	March 31, 2006	December 31, 2005
Assets		
Current assets:		
Cash and cash equivalents	\$ 41,457,805	\$ 20,844,640
Marketable securities	12,449,176	28,965,329
Accounts receivable, net	13,958,309	14,330,087
Deferred income taxes	717,000	717,000
Prepaid expenses and other current assets	1,601,087	1,227,586
Total current assets	70,183,377	66,084,642
Property and equipment, net	5,467,176	5,361,319
Deferred income taxes	10,409,000	8,949,000
Licensed technology, net	180,000	210,000
Other intangible assets, net	4,172,000	4,493,000
Goodwill	6,052,744	6,052,744
Total assets	\$ 96,464,297	\$ 91,150,705
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	\$ 1,815,918	\$ 2,639,608
Accrued compensation	2,517,001	3,687,866
Accrued royalties	1,056,200	1,347,660
Other current liabilities	1,070,988	1,575,215
Deferred revenue	11,774,759	11,230,578
Total current liabilities	18,234,866	20,480,927
Deferred revenue	1,046,596	645,230
Deferred rent	1,186,283	1,235,051
Total liabilities	20,467,745	22,361,208
Commitments and contingencies (Note 9)		
Stockholders' equity:		
Preferred stock: \$0.01 par value; 5,000,000 shares authorized; none issued or outstanding		
Common stock: \$0.01 par value; 20,000,000 shares authorized; 13,154,275 issued and outstanding as of March 31, 2006; and 12,847,744 issued and outstanding as of December 31, 2005	131,543	128,478
Additional paid-in capital	79,973,396	75,918,201
Deferred stock-based compensation		(1,707,013)
Accumulated deficit	(4,103,101)	(5,530,236)
Accumulated other comprehensive loss	(5,286)	(19,933)
Total stockholders' equity	75,996,552	68,789,497
Total liabilities and stockholders' equity	\$ 96,464,297	\$ 91,150,705

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

Vital Images, Inc.
Condensed Consolidated Income Statements
(Unaudited)

	For the Three Months Ended March 31,	
	2006	2005
Revenue:		
License fees	\$ 11,016,958	\$ 7,330,998
Maintenance and services	4,464,771	3,350,855
Hardware	314,300	643,075
Total revenue	15,796,029	11,324,928
Cost of revenue:		
License fees	1,242,780	1,080,700
Maintenance and services	1,744,785	1,226,036
Hardware	216,165	365,575
Total cost of revenue	3,203,730	2,672,311
Gross profit	12,592,299	8,652,617
Operating expenses:		
Sales and marketing	5,140,064	3,420,044
Research and development	3,021,162	1,778,161
General and administrative	2,506,476	1,590,387
Loss on operating lease		493,000
Total operating expenses	10,667,702	7,281,592
Operating income	1,924,597	1,371,025
Interest income	514,538	163,244
Income before income taxes	2,439,135	1,534,269
Provision for income taxes, net	1,012,000	511,000
Net income	\$ 1,427,135	\$ 1,023,269
Net income per share - basic	\$ 0.11	\$ 0.08
Net income per share - diluted	\$ 0.10	\$ 0.08
Weighted average common shares outstanding - basic	12,962,518	12,070,838
Weighted average common shares outstanding - diluted	13,862,036	12,953,393

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

Vital Images, Inc.
Condensed Consolidated Statements of Cash Flows
(Unaudited)

	For the Three Months Ended March 31,	
	2006	2005
Cash Flows From Operating Activities:		
Net income	\$ 1,427,135	\$ 1,023,269
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization of property and equipment	604,365	477,595
Amortization of identified intangible assets	351,000	351,000
Provision for (recovery of) doubtful accounts, net		(184,395)
Deferred income taxes	1,012,000	(248,000)
Tax benefit from stock option transactions (1)		759,000
Excess tax benefit from stock transactions (1)	(2,456,000)	
Amortization of discount and accretion of premium on marketable securities	(171,777)	107,314
Employee stock-based compensation	1,201,567	16,569
Non-employee stock-based compensation	5,003	1,418
Loss on operating lease		493,000
Amortization of deferred rent	(46,200)	(29,658)
Changes in operating assets and liabilities:		
Accounts receivable	371,778	(5,726,348)
Prepaid expenses and other current assets	(373,501)	(532,420)
Accounts payable	(716,715)	610,543
Accrued expenses and other liabilities	(2,128,121)	(1,570,403)
Deferred revenue	945,547	1,637,612
Deferred rent		1,180,354
Net cash provided by (used in) operating activities (1)	26,081	(1,633,550)
Cash Flows From Investing Activities:		
Purchases of property and equipment	(817,197)	(2,125,602)
Purchases of marketable securities	(988,423)	(3,065,359)
Maturities of marketable securities	17,700,000	3,034,830
Net cash provided by (used in) investing activities	15,894,380	(2,156,131)
Cash Flows From Financing Activities:		
Proceeds from sale of common stock under stock plans	2,236,704	1,075,650
Excess tax benefit from stock transactions (1)	2,456,000	
Net cash provided by financing activities (1)	4,692,704	1,075,650
Net Increase (Decrease) in Cash and Cash Equivalents	20,613,165	(2,714,031)
Cash and Cash Equivalents, Beginning of Period	20,844,640	24,119,157
Cash and Cash Equivalents, End of Period	\$ 41,457,805	\$ 21,405,126
Supplemental cash flow information:		
Purchases of property and equipment with accounts payable	\$ 201,078	\$ 751,792

(1) Prior to the adoption of SFAS 123(R), the Company presented all tax benefits resulting from the exercise of stock options and settlement of restricted stock awards as operating cash inflows in the consolidated statements of cash flows, in accordance with the provisions of the Emerging Issues Task Force (EITF) Issue No 00-15, Classification in the Statement of Cash Flows of the Income Tax Benefit Received by a Company upon Exercise of a Nonqualified Employee Stock Option. SFAS 123(R) requires the benefits of tax deductions in excess of the compensation cost recognized for those options and stock awards to be classified as financing cash inflows rather than operating cash inflows, on a prospective basis. See further discussion in Liquidity and capital resources Operating activities.

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

Vital Images, Inc.

Notes to Condensed Consolidated Financial Statements (Unaudited)

1. Basis of presentation

The accompanying unaudited consolidated financial statements of Vital Images, Inc. (the Company) have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and notes required by accounting principles generally accepted in the United States of America. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, for a fair statement, have been included. Operating results for the three months ended March 31, 2006 are not necessarily indicative of the results that may be expected for any subsequent quarter or for the year ending December 31, 2006. These financial statements should be read in conjunction with the financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2005.

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, HInnovation, Inc. All intercompany accounts and transactions have been eliminated. The Company views its operations and manages its business as one reportable segment—the development and marketing of software and related services for enterprise-wide advanced visualization and analysis solutions for use by medical professionals in clinical analysis and therapy planning. Factors used to identify the Company's single operating segment include the financial information available for evaluation by the chief operating decision maker in making decisions about how to allocate resources and assess performance. The Company markets its products and services through a direct sales force and independent distributors in the United States and international markets.

2. Major customer and geographic data

The following customers accounted for more than 10% of the Company's total revenue for the periods indicated:

	For the three months ended	
	March 31,	
	2006	2005
Toshiba Medical Systems Corporation	\$ 6,882,000	\$ 6,240,000
Percentage of total revenue	44%	55%
McKesson Information Systems LLC	\$ 1,703,000	\$ 921,000
Percentage of total revenue	11%	8%