

CRYO CELL INTERNATIONAL INC

Form 10-Q

April 14, 2015

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U.S. 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 February 28, 2015**

**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 0-23386

CRYO-CELL INTERNATIONAL, INC.

(Exact name of Registrant as Specified in its Charter)

DELAWARE
(State or other Jurisdiction of

22-3023093
(I.R.S. Employer

Incorporation or Organization)

Identification No.)

700 Brooker Creek Blvd. Oldsmar, FL 34677

(Address of Principal Executive Offices) (Zip Code)

Issuer's phone number, including area code: (813) 749-2100

(Former name, former address and former fiscal year, if changed since last report).

Check whether the registrant (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 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 Not Applicable

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

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

State the number of shares outstanding of each of the Registrant's classes of common stock, as of the latest practicable date.

As of April 8, 2015, 12,225,340 shares of \$0.01 par value common stock were issued and 9,916,306 were outstanding.

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CRYO-CELL INTERNATIONAL, INC. AND SUBSIDIARIES

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	February 28, 2015 (unaudited)	November 30, 2014
<u>ASSETS</u>		
<u>Current Assets</u>		
Cash and cash equivalents	\$ 3,550,243	\$ 3,279,267
Restricted cash	204,197	204,141
Marketable securities	98,261	102,674
Accounts receivable (net of allowance for doubtful accounts of \$2,032,416 and \$1,976,966, respectively)	4,200,003	4,071,997
Prepaid expenses	664,674	710,754
Other current assets	129,626	123,126
Total current assets	8,847,004	8,491,959
<u>Property and Equipment-net</u>	918,190	953,415
<u>Other Assets</u>		
Investment in Saneron CCEL Therapeutics, Inc.	684,000	684,000
Deposits and other assets, net	70,171	80,212
Total other assets	754,171	764,212
Total assets	\$ 10,519,365	\$ 10,209,586

LIABILITIES AND STOCKHOLDERS DEFICIT

<u>Current Liabilities</u>		
Accounts payable	\$ 1,335,709	\$ 992,910
Accrued expenses	907,075	1,471,699
Deferred revenue	6,460,146	6,662,552
Total current liabilities	8,702,930	9,127,161
<u>Other Liabilities</u>		
Deferred revenue, net of current portion	9,797,209	9,509,088
Long-term liability - revenue sharing agreements	2,300,000	2,300,000
Total other liabilities	12,097,209	11,809,088

Commitments and contingencies (Note 6)

Stockholders Deficit

Preferred stock (\$.01 par value, 500,000 authorized and none issued and outstanding), and Series A Junior participating preferred stock (\$.01 par value, 20,000 authorized and none issued and outstanding)		
Common stock (\$.01 par value, 20,000,000 authorized; 12,225,340 issued and 9,993,808 outstanding as of February 28, 2015 and 11,921,285 issued and 9,706,174 outstanding as of November 30, 2014)	119,213	119,213
Additional paid-in capital	28,040,867	27,842,106
Treasury stock, at cost	(5,151,690)	(5,112,648)
Accumulated deficit	(33,289,164)	(33,575,334)
Total stockholders deficit	(10,280,774)	(10,726,663)
Total liabilities and stockholders deficit	\$ 10,519,365	\$ 10,209,586

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

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CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

	For the Three Months Ended	
	February 28, 2015	February 28, 2014
Revenue:		
Processing and storage fees	\$ 4,673,969	\$ 4,357,231
Licensee income	169,412	963,251
Total revenue	4,843,381	5,320,482
Costs and Expenses:		
Cost of sales	1,273,987	1,334,361
Selling, general and administrative expenses	2,913,973	3,122,723
Research, development and related engineering	11,988	14,368
Depreciation and amortization	18,242	44,505
Total costs and expenses	4,218,190	4,515,957
Operating Income	625,191	804,525
Other Income (Expense):		
Other income (expense)	(4,075)	27,769
Interest expense	(301,286)	(274,316)
Total other expense	(305,361)	(246,547)
Income before equity in losses of affiliate and income tax expense	319,830	557,978
Equity in losses of affiliate	(8,248)	(113,575)
Income before income tax expense	311,582	444,403
Income tax expense	(25,412)	(47,291)
Net Income	\$ 286,170	\$ 397,112
Net income per common share - basic	\$ 0.03	\$ 0.04

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Weighted average common shares outstanding - basic	9,824,566	10,690,188
Net income per common share - diluted	\$ 0.03	\$ 0.04
Weighted average common shares outstanding - diluted	10,058,649	10,764,158

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

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CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	For the Three Months Ended	
	February 28, 2015	February 28, 2014
Net income	\$ 286,170	\$ 397,112
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization expense	58,994	95,813
Compensatory element of stock options	190,513	152,236
Provision for doubtful accounts	140,505	161,891
Equity in losses of affiliate	8,248	113,575
Changes in assets and liabilities:		
Accounts receivable	(268,511)	(529,649)
Notes receivable		550,782
Prepaid expenses and other current assets	46,080	77,758
Other current assets	(6,500)	
Deposits and other assets, net	9,575	42,628
Accounts payable	342,799	231,176
Accrued expenses	(564,624)	(713,994)
Deferred revenue	85,715	(686,024)
Net cash provided by (used in) operating activities	328,964	(106,696)
Cash flows from investing activities:		
Release of restricted cash held in escrow	(56)	24,166
Purchases of property and equipment	(23,303)	(11,025)
Sales (purchases) of marketable securities and other investments, net	4,413	(61,685)
Investment in affiliate		(75,000)
Net cash used in investing activities	(18,946)	(123,544)
Cash flows from financing activities:		
Treasury stock purchases	(39,042)	(451,913)
Net cash used in financing activities	(39,042)	(451,913)
Increase (decrease) in cash and cash equivalents	270,976	(682,153)
Cash and cash equivalents - beginning of period	3,279,267	3,925,156

Cash and cash equivalents - end of period	\$ 3,550,243	\$ 3,243,003
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The accompanying notes are an integral part of these consolidated financial statements.

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CRYO-CELL INTERNATIONAL, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

February 28, 2015

(Unaudited)

Note 1 - Basis of Presentation and Significant Accounting Policies

The unaudited consolidated financial statements including the Consolidated Balance Sheets as of February 28, 2015 and November 30, 2014, the related Consolidated Statements of Operations and Cash Flows for the three months ended February 28, 2015 and 2014 have been prepared by Cryo-Cell International, Inc. and its subsidiaries (the Company or Cryo-Cell) pursuant to the rules and regulations of the Securities and Exchange Commission for interim financial reporting. Certain financial information and note disclosures, which are normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States of America, have been condensed or omitted pursuant to those rules and regulations. It is suggested that these consolidated financial statements be read in conjunction with the financial statements and notes thereto included in the Company's November 30, 2014 Annual Report on Form 10-K. In the opinion of management, all adjustments (which include only normal recurring adjustments) necessary to present fairly the financial position, results of operations, and changes in cash flows for all periods presented have been made. The results of operations for the three months ended February 28, 2015 are not necessarily indicative of the results expected for any interim period in the future or the entire year ending November 30, 2015.

Revenue Recognition

Revenue Recognition for Arrangements with Multiple Deliverables

For multi-element arrangements, the Company allocates revenue to all deliverables based on their relative selling prices. In such circumstances, accounting principles establish a hierarchy to determine the selling price to be used for allocating revenue to deliverables as follows: (i) vendor-specific objective evidence of fair value (VSOE), (ii) third-party evidence of selling price (TPE), and (iii) best estimate of the selling price (ESP). VSOE generally exists only when the Company sells the deliverable separately and it is the price actually charged by the Company for that deliverable.

The Company has identified two deliverables generally contained in the arrangements involving the sale of its umbilical cord blood product. The first deliverable is the processing of a specimen. The second deliverable is either the annual storage of a specimen, the 21-year storage fee charged for a specimen or the life-time storage fee charged for a specimen. The Company has allocated revenue between these deliverables using the relative selling price method. The Company has VSOE for its annual storage fees as the Company renews storage fees annually with its customers on a stand-alone basis. Because the Company has neither VSOE nor TPE for the processing, 21-year storage and life-time storage deliverables, the allocation of revenue has been based on the Company's ESPs. Amounts allocated to processing a specimen are recognized at the time the processing of the specimen is complete. Amounts allocated to the storage of a specimen are recognized ratably over the contractual storage period. Any discounts given to the customer are recognized by applying the relative selling price method whereby after the Company determines the selling price to be allocated to each deliverable (processing and storage), the sum of the prices of the deliverables is then compared to the arrangement consideration, and any difference is applied to the separate deliverables ratably.

The Company's process for determining its ESP for deliverables without VSOE or TPE considers multiple factors that may vary depending upon the unique facts and circumstances related to each deliverable. Key factors considered by the Company in developing the ESPs for its processing, 21 year storage and life-time storage fee include the Company's historical pricing practices as well as expected profit margins.

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The Company records revenue from processing and storage of specimens and pursuant to agreements with licensees. The Company recognizes revenue from processing fees upon completion of processing and recognizes storage fees ratably over the contractual storage period as well as other income from royalties paid by licensees related to long-term storage contracts which the Company has under license agreements. Contracted storage periods are annual, twenty-one years and lifetime. Deferred revenue on the accompanying consolidated balance sheets includes the portion of the annual storage fee, the twenty-one year storage fee and the life-time storage fee that is being recognized over the contractual storage period as well as royalties received from foreign licensees related to long-term storage contracts in which the Company has future obligations under the license agreement. The Company classifies deferred revenue as current if the Company expects to recognize the related revenue over the next 12 months. The Company also records revenue within processing and storage fees from shipping and handling billed to customers when earned. Shipping and handling costs that the Company incurs are expensed and included in cost of sales.

Income Taxes

Deferred income tax assets and liabilities are recognized for the estimated future tax consequences attributable to differences between financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred income tax assets and liabilities are measured using enacted tax rates expected to be recovered or settled. The Company has recorded a valuation allowance of \$10,332,000 and \$10,517,000 as of February 28, 2015 and November 30, 2014, respectively, as the Company does not believe it is more likely than not that all future income tax benefits will be realized. When the Company changes its determination as to the amount of deferred income tax assets that can be realized, the valuation allowance is adjusted with a corresponding impact to income tax expense in the period in which such determination is made. The ultimate realization of the Company's deferred income tax assets depends upon generating sufficient taxable income prior to the expiration of the tax attributes. In assessing the need for a valuation allowance, the Company projects future levels of taxable income. This assessment requires significant judgment. The Company examines the evidence related to the recent history of losses, the economic conditions in which the Company operates and forecasts and projections to make that determination.

There was no U.S. income tax expense for the three months ended February 28, 2015 and February 28, 2014 due to the utilization of net operating losses and foreign tax credit carryforwards, which were not previously benefited in the Company's financial statements.

The Company records foreign income taxes withheld from installment payments of non-refundable up-front license fees and royalty income earned on the processing and storage of cord blood stem cell specimens in geographic areas where the Company has license agreements. The Company recognized approximately \$25,000 and \$47,000 for the three months ended February 28, 2015 and February 28, 2014, respectively, of foreign income tax expense. Foreign income tax expense is included in income tax expense in the accompanying consolidated statements of operations.

The Company recognizes the financial statement benefit of a tax position only after determining that the relevant tax authority would more likely than not sustain the position following an audit. For tax positions meeting the more-likely-than-not threshold, the amount recognized in the financial statements is the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement with the relevant tax authority. Increases or decreases to the unrecognized tax

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benefits could result from management's belief that a position can or cannot be sustained upon examination based on subsequent information or potential lapse of the applicable statute of limitation for certain tax positions.

The Company recognizes interest and penalties related to uncertain tax positions in income tax expense. For the three months ended February 28, 2015 and February 28, 2014, the Company had no provisions for interest or penalties related to uncertain tax positions.

Long-Lived Assets

The Company evaluates the realizability of its long-lived assets, which requires impairment losses to be recorded on long-lived assets used in operations when indicators of impairment, such as reductions in demand or when significant economic slowdowns are present. Reviews are performed to determine whether the carrying value of an asset is impaired, based on comparisons to undiscounted expected future cash flows. If this comparison indicates that there is impairment and carrying value is in excess of fair value, the impaired asset is written down to fair value, which is typically calculated using: (i) quoted market prices or (ii) discounted expected future cash flows utilizing a discount rate. The Company did not note any impairment for the three months ended February 28, 2015 and 2014.

Stock Compensation

As of February 28, 2015, the Company has three stock-based compensation plans, which are described in Note 4 to the consolidated financial statements. The Company's third stock-based employee compensation plan became effective December 1, 2011 as approved by the Board of Directors and approved by the stockholders at the 2012 Annual Meeting. The Company recognized approximately \$191,000 and \$152,000 for the three months ended February 28, 2015 and February 28, 2014, respectively, of stock-based compensation expense.

The Company recognizes stock-based compensation based on the fair value of the related awards. Under the fair value recognition guidance of stock-based compensation accounting rules, stock-based compensation expense is estimated at the grant date based on the fair value of the award and is recognized as expense over the requisite service period of the award. The fair value of service-based vesting condition and performance-based vesting condition stock option awards is determined using the Black-Scholes valuation model. For stock option awards with only service-based vesting conditions and graded vesting features, the Company recognizes stock compensation expense based on the graded-vesting method. The Company recognizes compensation cost for awards with market-based vesting conditions on a graded-vesting basis over the derived service period calculated by the binomial valuation model. The use of these valuation models involve assumptions that are judgmental and highly sensitive in the determination of compensation expense and include the expected life of the option, stock price volatility, risk-free interest rate, dividend yield, exercise price, and forfeiture rate. Forfeitures are estimated at the time of valuation and reduce expense ratably over the vesting period.

The estimation of stock awards that will ultimately vest requires judgment and to the extent that actual results or updated estimates differ from current estimates, such amounts will be recorded as a cumulative adjustment in the period they become known. The Company considered many factors when estimating forfeitures, including the recipient groups and historical experience. Actual results and future changes in estimates may differ substantially from current estimates.

Performance-based equity awards vest upon the achievement of certain financial performance goals, including revenue and income targets. Determining the appropriate amount to expense based on the anticipated achievement of the stated goals requires judgment, including forecasting future financial

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results. The estimate of the timing of the expense recognition is revised periodically based on the probability of achieving the required performance targets and adjustments are made as appropriate. The cumulative impact of any revision is reflected in the period of the change. If the financial performance goals are not met, the award does not vest, so no compensation cost is recognized and any previously recognized stock-based compensation expense is reversed.

Equity awards with market-based vesting conditions vest upon the achievement of certain stock price targets. If the awards are forfeited prior to the completion of the derived service period, any recognized compensation is reversed. If the awards are forfeited after the completion of the derived service period, the compensation cost is not reversed, even if the awards never vest.

Fair Value of Financial Instruments

Management uses a fair value hierarchy, which gives the highest priority to quoted prices in active markets. The fair value of financial instruments is estimated based on market trading information, where available. Absent published market values for an instrument or other assets, management uses observable market data to arrive at its estimates of fair value. Management believes that the carrying amount of cash and cash equivalents, accounts receivable, notes receivable, accounts payable and accrued expenses approximate fair value. The Company believes that the fair value of its revenue sharing agreements liability recorded on the balance sheet is between the recorded book value and up to the Company's settlement experience, due to the various terms and conditions associated with each Revenue Sharing Agreement.

The Company uses an accounting standard that defines fair value as an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. As a basis for considering such assumptions, the standard establishes a three-level fair value hierarchy that prioritizes the inputs used to measure fair value. The three levels of inputs used to measure fair value are as follows:

- Level 1 Quoted prices in active markets for identical assets or liabilities.
- Level 2 Observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.
- Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. This includes certain pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs.

The following table summarizes the financial assets and liabilities measured at fair value on a recurring basis as of February 28, 2015 and November 30, 2014, respectively, segregated among the appropriate levels within the fair value hierarchy:

Description	Fair Value at February 28, 2015	Fair Value Measurements at February 28, 2015 Using		
		Level 1	Level 2	Level 3
Assets:				
Trading Securities	\$ 98,261	\$ 98,261		

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Description	Fair Value at November 30, 2014	Fair Value Measurements at November 30, 2014 Using		
		Level 1	Level 2	Level 3
Assets:				
Trading Securities	\$ 102,674	\$ 102,674		

The following is a description of the valuation techniques used for these items, as well as the general classification of such items pursuant to the fair value hierarchy:

Trading securities Fair values for these investments are based on quoted prices in active markets and are therefore classified within Level 1 of the fair value hierarchy.

There was (\$4,400) and \$15,525 in unrealized holding loss and gain, respectively, recorded in other income and expense on the accompanying consolidated statements of operations for the three months ended February 28, 2015 and 2014.

Product Warranty and Cryo-Cell Cares™ Program

In December 2005, the Company began providing its customers that enrolled after December 2005 a payment warranty under which the Company agrees to pay \$50,000 to its client if the umbilical cord blood product retrieved is used for a stem cell transplant for the donor or an immediate family member and fails to engraft, subject to various restrictions. Effective February 1, 2012, the Company increased the \$50,000 payment warranty to a \$75,000 payment warranty to all of its new clients. Additionally, under the Cryo-Cell Cares™ program, the Company was paying \$10,000 to the client to offset personal expenses if the umbilical cord blood product is used for bone marrow reconstitution in a myeloblastic transplant procedure. Effective October 13, 2014, the Company no longer offers the Cryo-Cell Cares™ program to new clients. The product warranty is available to clients who enroll under this structure for as long as the specimen is stored with the Company. The Company has not experienced any claims under the warranty program nor has it incurred costs related to these warranties. The Company does not maintain insurance for this warranty program and therefore maintains reserves to cover any estimated potential liabilities. The Company's reserve balance is based on the \$75,000 or \$50,000 (as applicable) maximum payment and the \$10,000 maximum expense reimbursement multiplied by formulas to determine the projected number of units requiring a payout. The Company determined the estimated expected usage and engraftment failure rates based on an analysis of the historical usage and failure rates and the historical usage and failure rates in other private and public cord blood banks based on published data. The Company's estimates of expected usage and engraftment failure could change as a result of changes in actual usage rates or failure rates and such changes would require an adjustment to the established reserves. The historical usage and failure rates have been very low and a small increase in the number of transplants or engraftment failures could cause a significant increase in the estimated rates used in determining the Company's reserve. In addition, the reserve will increase as additional umbilical cord blood specimens are stored which are subject to the warranty. As of February 28, 2015 and November 30, 2014 the Company recorded reserves under these programs in the amounts of approximately \$17,000 and \$17,000, respectively, which are included in accrued expenses in the accompanying consolidated balance sheets.

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In June 2014, the FASB issued Accounting Standards Update No. 2014-12, *Compensation – Stock Compensation (Topic 718): Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could be Achieved after the Requisite Service Period* (ASU 2014-12). This update requires that a performance target that affects vesting, and that could be achieved after the requisite service period, be treated as a performance condition in determining expense recognition for the award. As a result, this type of performance condition may delay expense recognition until achievement of the performance target is probable. ASU 2014-12 is effective for reporting periods beginning after December 15, 2015, and early adoption is permitted. We will adopt ASU 2014-12 effective December 1, 2016 and it is not anticipated to have a material impact on our financial statements.

In May 2014, the FASB issued Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*. This update provides a comprehensive new revenue recognition model that requires a company to recognize revenue to depict the transfer of goods or services to a customer at an amount that reflects the consideration it expects to receive in exchange for those goods or services. The guidance also requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts. This update is effective for annual and interim periods beginning after December 15, 2016, which will require us to adopt these provisions in the first quarter of fiscal 2018. Early application is not permitted. This update permits the use of either the retrospective or cumulative effect transition method. We are evaluating the effect this guidance will have on our consolidated financial statements and related disclosures. We have not yet selected a transition method nor have we determined the effect of the standard on our ongoing financial reporting.

Note 2 Income per Common Share

Net income per common share data are based on net income. The following table sets forth the calculation of basic and diluted earnings per share:

	For the three months ended February 28, 2015	For the three months ended February 28, 2014
Numerator:		
Net Income	\$ 286,170	\$ 397,112