

SOCKET MOBILE, INC.
Form 10-Q
August 13, 2013

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2013

OR

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

For the transition period _____ to _____.

Commission file number 1-13810

SOCKET MOBILE, INC.

(Exact name of registrant as specified in its charter)

Delaware **94-3155066**
(State of incorporation) (IRS Employer Identification No.)

39700 Eureka Drive, Newark, CA 94560

(Address of principal executive offices including zip code)

(510) 933-3000

(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.

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

The number of shares of Common Stock (\$0.001 par value) outstanding as of August 9, 2013 was 4,867,063 shares.

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Index**PART I****Item 1. Financial Statements**SOCKET MOBILE, INC.
CONDENSED BALANCE SHEETS

	June 30, 2013 (Unaudited)	December 31, 2012
ASSETS		
Current assets:		
Cash and cash equivalents	\$659,834	\$390,513
Accounts receivable, net	2,469,574	1,509,094
Inventories	1,032,166	941,067
Prepaid expenses and other current assets	119,457	129,434
Total current assets	4,281,031	2,970,108
Property and equipment:		
Machinery and office equipment	1,827,487	1,865,137
Computer equipment	1,146,240	1,204,957
	2,973,727	3,070,094
Accumulated depreciation	(2,677,228)	(2,727,323)
Property and equipment, net	296,499	342,771
Intangible assets, net	60,000	90,000
Goodwill	4,427,000	4,427,000
Other assets	91,518	91,518
Total assets	\$9,156,048	\$7,921,397
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and accrued expenses	\$3,713,192	\$3,771,763
Accrued payroll and related expenses	560,981	478,084
Bank line of credit	1,145,053	810,686
Deferred income on shipments to distributors	1,024,275	854,159
Related party and other short term notes payable	550,000	95,289
Related party convertible notes payable	725,000	750,000
Short term portion of deferred service revenue	198,567	214,537
Short term portion of capital leases and deferred rent	22,555	17,400
Total current liabilities	7,939,623	6,991,918
Long term portion of deferred service revenue	120,794	153,877
Long term portion of capital leases and deferred rent	254,998	227,022

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Deferred income taxes	95,365	79,395
Total liabilities	8,410,780	7,452,212
Commitments and contingencies		
Stockholders' equity:		
Common stock, \$0.001 par value: Authorized – 20,000,000 shares, Issued and outstanding – 4,867,063 shares at June 30, 2013 and 4,861,063 at December 31, 2012	4,867	4,861
Additional paid-in capital	61,124,271	60,966,505
Accumulated deficit	(60,383,870)	(60,502,181)
Total stockholders' equity	745,268	469,185
Total liabilities and stockholders' equity	\$9,156,048	\$7,921,397

See accompanying notes.

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SOCKET MOBILE, INC.
 CONDENSED STATEMENTS OF OPERATIONS
 (Unaudited)

	Three Months Ended		Six Months Ended	
	June 30, 2013	2012	June 30, 2013	2012
Revenues	\$4,435,431	\$4,037,502	\$8,700,606	\$7,991,261
Cost of revenues	2,630,841	2,539,251	5,187,931	4,969,941
Gross profit	1,804,590	1,498,251	3,512,675	3,021,320
Operating expenses:				
Research and development	594,140	739,860	1,118,890	1,523,905
Sales and marketing	585,088	982,405	1,144,287	1,942,432
General and administrative	448,695	496,541	909,757	1,109,699
Total operating expenses	1,627,923	2,218,806	3,172,934	4,576,036
Operating income (loss)	176,667	(720,555)	339,741	(1,554,716)
Interest expense and other, net	(125,173)	(26,860)	(205,460)	(56,488)
Net income (loss) before income taxes	51,494	(747,415)	134,281	(1,611,204)
Income tax expense	(7,985)	(7,985)	(15,970)	(15,970)
Net income (loss)	\$43,509	\$(755,400)	\$118,311	\$(1,627,174)
Net income (loss) per share:				
Basic	\$0.01	\$(0.16)	\$0.02	\$(0.34)
Diluted	\$0.01	\$(0.16)	\$0.02	\$(0.34)
Weighted average shares outstanding:				
Basic	4,864,953	4,854,179	4,863,008	4,846,197
Diluted	4,987,156	4,854,179	4,946,155	4,846,197

See accompanying notes.

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SOCKET MOBILE, INC.
 CONDENSED STATEMENTS OF CASH FLOWS
 (Unaudited)

	Six Months Ended June 30,	
	2013	2012
Operating activities		
Net income (loss)	\$ 118,311	\$(1,627,174)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Stock-based compensation	151,292	363,460
Depreciation and amortization	132,732	183,303
Deferred income tax expense	15,970	15,970
Changes in operating assets and liabilities:		
Accounts receivable	(960,480)	1,285,061
Inventories	(91,099)	(304,602)
Prepaid expenses and other current assets	9,977	58,608
Other assets	—	(1,442)
Accounts payable	(58,570)	417,088
Accrued payroll and related expenses	82,897	43,383
Deferred income on shipments to distributors	170,116	(402,354)
Deferred service revenue	(49,054)	12,314
Change in deferred rent	28,187	(8,043)
Net cash (used in) provided by operating activities	(449,721)	35,572
Investing activities		
Purchases of equipment	(41,860)	(205,827)
Net cash used in investing activities	(41,860)	(205,827)
Financing activities		
Payments on capital leases	(9,656)	(6,202)
Proceeds from borrowings under bank line of credit agreement	4,422,333	3,896,718
Repayments of borrowings under bank line of credit agreement	(4,087,966)	(4,108,903)
Stock options exercised	6,480	14,015
Warrants exercised	—	29,999
Proceeds from the issuance of related party and other short term notes payable	550,000	—
Repayment of short term note payable	(95,289)	—
Redemption of related party convertible note payable	(25,000)	—
Net cash provided by (used in) financing activities	760,902	(174,373)
Net increase (decrease) in cash and cash equivalents	269,321	(344,628)
Cash and cash equivalents at beginning of period	390,513	957,022

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Cash and cash equivalents at end of period	\$659,834	\$612,394
Supplemental cash flow information		
Cash paid for interest	\$163,998	\$61,319

See accompanying notes.

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SOCKET MOBILE, INC.

NOTES TO CONDENSED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1 — Basis of Presentation

The accompanying unaudited condensed financial statements of Socket Mobile, Inc. (the “Company”) have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Article 8 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, all adjustments, consisting only of normal recurring accruals considered necessary for fair presentation have been included. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted.

These condensed financial statements should be read in conjunction with the audited financial statements and notes included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2012. The financial statements in the Company’s annual report on Form 10-K were prepared on a going concern basis.

Liquidity and Going Concern

The Company was profitable in each of the first two quarters in 2013, but only to the extent of \$118,311 in total. In the year ended December 31, 2012, the Company incurred a net loss of \$3,298,082. As of June 30, 2013, the Company has an accumulated deficit of \$60,383,870. The Company’s cash balances at June 30, 2013 were \$659,834, including \$1,145,053 advanced on its bank lines of credit. At June 30, 2013, the Company had additional unused borrowing capacity of approximately \$410,000 on its bank lines of credit. The Company’s balance sheet at June 30, 2013 has a current ratio (current assets divided by current liabilities) of 0.5 to 1.0, and a working capital deficit of \$3,658,592 (current assets less current liabilities). These circumstances raise substantial doubt about the Company’s ability to continue as a going concern.

In the last three years the Company has taken actions to reduce its expenses and to align its cost structure with economic conditions. The Company has the ability to further reduce expenses if necessary. Steps taken by the

Company to reduce operating losses and achieve profitability include reduction of headcount to manage payroll costs, the introduction of new products, and continued close support of the Company's distributors and application development partners as they establish their mobile applications in key vertical markets. The Company completed additional financing during the first quarter of 2013 (see "NOTE 5 — Related Party and Other Short Term Notes Payable" for more information). The Company believes it will be able to further improve its liquidity and secure additional sources of financing by managing its working capital balances, use of its bank lines of credit, and raising additional capital as needed including development funding from development partners and the issuance of additional equity securities. However, there can be no assurance that additional capital will be available on acceptable terms, if at all, and any such terms may be dilutive to existing stockholders. The Company's bank lines of credit may be terminated by the bank or by the Company at any time, and expire on October 11, 2013 unless renewed (see "NOTE 6 — Bank Financing Arrangements"). If the Company cannot maintain profitability, it will not be able to support its operations from positive cash flows, and would use its existing cash to support operating losses. If the Company is unable to secure the necessary capital for its business, it may need to suspend some or all of its current operations.

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SOCKET MOBILE, INC.

NOTES TO CONDENSED FINANCIAL STATEMENTS

(Unaudited)

If the Company can maintain revenue growth and attain ongoing profitability, it anticipates requirements for cash will include funding of higher receivable and inventory balances, and increased expenses, including an increase of costs relating to new employees to support our growth and increases in salaries, benefits, and related support costs for employees.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern, which contemplates the realization of assets and the settlement of liabilities and commitments in the normal course of business. These financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classification of liabilities that may result from the Company's inability to continue as a going concern.

NOTE 2 — Summary of Significant Accounting Policies

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expense during the reporting period. Actual results could differ from those estimates, and such differences may be material to the financial statements.

Cash Equivalents and Fair Value of Financial Instruments

The Company considers all highly liquid investments purchased with an original maturity date of 90 days or less at date of purchase to be cash equivalents. At June 30, 2013 and December 31, 2012, all of the Company's cash and cash equivalents consisted of amounts held in demand and money market deposits in banks. The carrying value of the Company's cash and cash equivalents, accounts receivable, accounts payable, debt and foreign exchange contracts approximate fair value due to the relatively short period of time to maturity.

NOTE 3 — Inventories

Inventories consist principally of raw materials and sub-assemblies, which are stated at the lower of cost (first-in, first-out) or market.

	June 30, 2013	December 31, 2012
Raw materials and sub-assemblies	\$957,083	\$921,677
Finished goods	75,083	19,390
	\$1,032,166	\$941,067

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SOCKET MOBILE, INC.

NOTES TO CONDENSED FINANCIAL STATEMENTS

(Unaudited)

NOTE 4 — Related Party Convertible Notes Payable

On August 1, 2012, the Company issued to select officers and directors of the Company \$400,000 in convertible subordinated notes. The net proceeds of \$400,000 are being used for working capital purposes. The notes have a term of two years that accrue interest at 8% per annum and mature on August 1, 2014. Accrued interest is payable upon redemption. The notes and accrued interest may be redeemed after six months. The notes are convertible into common stock at the option of the holder at \$2.44 per share as long as warrants previously issued to Hudson Bay Capital Master Fund are outstanding, or at \$2.00 per share if the Hudson Bay warrants are no longer outstanding. The Hudson Bay Capital Master Fund warrants expire on May 20, 2016. The notes are secured by all of the assets of the Company and are subordinated to amounts outstanding under the Company's working capital bank line of credit with Silicon Valley Bank. During the quarter ended June 30, 2013, \$25,000 of these convertible notes were redeemed, resulting in a balance of \$375,000 outstanding at June 30, 2013.

On November 5, 2012, the Company's Board of Directors approved the issue of up to \$350,000 in convertible subordinated notes to its Chairman to be used for working capital purposes. At various dates beginning November 7, 2012 through December 12, 2012 the Company issued in total \$350,000 of such notes to its Chairman. The notes are identical to the notes issued on August 1, 2012 as described above. The notes are two-year notes that accrue interest at 8% and mature on August 1, 2014. Accrued interest is payable upon redemption. The notes and accrued interest may be redeemed after six months. The notes are convertible into common stock at the option of the holder at \$2.44 per share as long as warrants previously issued to Hudson Bay Capital Master Fund are outstanding, or at the fair market value per share at the time each note was issued if the Hudson Bay Warrants are no longer outstanding. The weighted average fair market value conversion price is \$1.04 per share. The notes are secured by all of the assets of the Company and are subordinated to amounts outstanding under the Company's working capital bank line of credit with Silicon Valley Bank.

Accrued interest expense at June 30, 2013 related to all convertible subordinated notes outstanding was \$44,734.

NOTE 5 — Related Party and Other Short Term Notes Payable

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On January 31, 2013, the Company's Board of Directors approved a subordinated line of credit of up to \$1,000,000. The term of the credit agreement is six months ending August 1, 2013, unless extended by both parties. Interest accrues at the rate of 1% per week and is to be paid weekly. Balances outstanding under the line of credit are to be repaid in full on or before the maturity date. Balances under the line of credit are secured by all of the assets of the Company and are subordinated to amounts outstanding under the Company's working capital bank line of credit