KOPIN CORP
Form 10-Q
May 10, 2018

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, 2018
¨ 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 0-19882

KOPIN CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	04-2833935
State or other jurisdiction of incorporation or organization	(I.R.S. Employer Identification No.)
125 North Drive, Westborough, MA	01581-3335
(Address of principal executive offices)	(Zip Code)

Registrant’s telephone number, including area code: (508) 870-5959

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 filing requirements for the past 90 days. Yes x 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 x 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 definitions of “large accelerated filer”, “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act) Yes ¨ No x
Indicate the number of shares outstanding of each issuer’s classes of common stock, as of the latest practicable date.

Class	Outstanding as of May 7, 2018
Common Stock, par value $0.01	76,529,535

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Part 1. FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements (Unaudited)
KOPIN CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

	March 31, 2018	December 30, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	$24,167,900	$24,848,227
Marketable debt securities, at fair value	36,873,595	43,907,457
Accounts receivable, net of allowance of $273,000 in 2018 and $149,000 in 2017	2,457,904	3,955,123
Contract assets - unbilled receivables	2,479,062	704,863
Inventory	3,773,305	5,080,797
Prepaid taxes	102,462	264,352
Prepaid expenses and other current assets	1,155,303	978,677
Total current assets	71,009,531	79,739,496
Property, plant and equipment, net	5,304,135	5,077,043
Goodwill	1,801,988	1,780,247
Intangible assets, net	662,727	883,636
Other assets	4,194,219	3,842,068
Equity investment	3,900,000	—
Total assets	$86,872,600	$91,322,490
LIABILITIES AND STOCKHOLDERS’ EQUITY		
Current liabilities:		
Accounts payable	$3,210,639	$4,918,605
Accrued payroll and expenses	1,920,873	1,636,512
Accrued warranty	599,000	649,000
Contract liabilities - billings in excess of revenue earned	384,073	896,479
Other accrued liabilities	2,106,782	2,066,025
Income tax payable	—	1,416,892
Deferred tax liabilities	523,529	520,000
Total current liabilities	8,744,896	12,103,513
Deferred revenue, net of current portion	262,207	374,171
Asset retirement obligations	280,348	269,877
Other long-term obligations	1,484,713	1,195,082
Stockholders’ equity:		
Preferred stock, par value $.01 per share: authorized, 3,000 shares; none issued	—	—
Common stock, par value $.01 per share: authorized, 120,000,000 shares; issued 81,046,313 shares in 2018 and 80,201,313 shares in 2017; outstanding 73,078,783 shares in 2018 and 73,058,783 shares in 2017	775,920	775,720
Additional paid-in capital	332,518,555	331,119,340
Treasury stock (4,513,256 shares in 2018 and 2017, at cost)	(17,238,669)	(17,238,669)
Accumulated other comprehensive income	3,294,916	3,564,779
Accumulated deficit	(242,598,797)	(240,121,901)
Total Kopin Corporation stockholders’ equity	76,751,925	78,099,269

Noncontrolling interest	(651,489)	(719,422)
Total stockholders' equity	76,100,436	77,379,847
Total liabilities and stockholders' equity	$86,872,600	$91,322,490

See notes to unaudited condensed consolidated financial statements

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KOPIN CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three months ended	
	March 31, 2018	April 1, 2017
Revenues:		
Net product revenues	$5,044,809	$3,933,142
Research and development revenues	608,811	444,985
	5,653,620	4,378,127
Expenses:		
Cost of product revenues	4,062,191	3,117,357
Research and development	4,451,653	4,281,870
Selling, general and administration	6,931,410	5,641,684
	15,445,254	13,040,911
Loss from operations	(9,791,634)	(8,662,784)
Other income (expense):		
Interest income	159,851	233,777
Other income	1,101,255	534,411
Foreign currency transaction gains (losses)	208,608	(1,191,283)
Gain on investments	2,849,816	—
	4,319,530	(423,095)
Loss before (provision) benefit for income taxes and net loss (income) attributable to noncontrolling interest	(5,472,104)	(9,085,879)
Tax benefit	—	1,146,000
Net loss	(5,472,104)	(7,939,879)
Net (income) loss attributable to noncontrolling interest	(64,174)	81,438
Net loss attributable to Kopin Corporation	$(5,536,278)	$(7,858,441)
Net loss per share		
Basic and diluted	$(0.08)	$(0.12)
Weighted average number of common shares outstanding		
Basic and diluted	73,078,344	64,538,686

See notes to unaudited condensed consolidated financial statements

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KOPIN CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(Unaudited)

	Three months ended	
	March 31, 2018	April 1, 2017
Net loss	$(5,472,104)	$(7,939,879)
Other comprehensive (loss) income, net of tax:		
Foreign currency translation adjustments	(124,480)	1,597,406
Unrealized holding losses on marketable securities	(136,874)	(11,314)
Reclassification of holding losses in net loss	(4,750)	(1,156)
Other comprehensive (loss) income, net of tax	(266,104)	1,584,936
Comprehensive loss	$(5,738,208)	$(6,354,943)
Comprehensive (income) loss attributable to the noncontrolling interest	(67,933)	58,034
Comprehensive loss attributable to controlling interest	$(5,806,141)	$(6,296,909)

See notes to unaudited condensed consolidated financial statements

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KOPIN CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(Unaudited)

	Common Stock				Accumulated		Total Kopin	
	Shares	Amount	Additional Paid-in Capital	Treasury Stock	Other Comprehensive Income	Accumulated Deficit	Corporation Stockholders' Equity	Noncontro Interest
Balance, December 30, 2017	77,572,038	$775,720	$331,119,340	$(17,238,669)	$3,564,779	$(240,121,901)	$78,099,269	$(719,422
Stock-based compensation	—	—	1,399,415	—	—	—	1,399,415	—
Vesting of restricted stock	20,000	200	(200)	—	—	—	—	—
Other comprehensive (loss) income	—	—	—	—	(269,863)	—	(269,863)	3,759
Adoption of accounting standards (Note 2)	—	—	—	—	—	3,059,382	3,059,382	—
Net loss	—	—	—	—	—	(5,536,278)	(5,536,278)	64,174
Balance, March 31, 2018	77,592,038	$775,920	$332,518,555	$(17,238,669)	$3,294,916	$(242,598,797)	$76,751,925	$(651,489

See notes to unaudited condensed consolidated financial statements

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KOPIN CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Three months ended	
	March 31, 2018	April 1, 2017
Cash flows from operating activities:		
Net loss	$(5,472,104)	$(7,939,879)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	554,967	443,174
Stock-based compensation	1,399,415	1,292,105
Foreign currency (gains) losses	(218,943)	1,190,199
Change in allowance for bad debt	(136,095)	—
Unrealized gain on investments	(2,849,816)	(274,000)
Deferred income taxes	—	(1,168,962)
Other non-cash items	442,691	157,140
Changes in assets and liabilities, net of acquired assets and liabilities:		
Accounts receivable	1,461,884	(210,823)
Contract assets	1,124,634	—
Inventory	(198,961)	(249,340)
Prepaid expenses and other current assets	98,008	(22,082)
Accounts payable and accrued expenses	(2,644,054)	10,736
Billings in excess of revenue earned	379,330	152,797
Net cash used in operating activities	(6,059,044)	(6,618,935)
Cash flows from investing activities:		
Other assets	(87,632)	(12,346)
Capital expenditures	(553,793)	(297,983)
Proceeds from sale of marketable debt securities	6,909,855	13,519,291
Cash paid for equity investment	(1,000,000)	—
Purchase of marketable debt securities	—	(948,637)
Cash paid for acquisition, net of cash acquired	—	(3,247,397)
Net cash provided by investing activities	5,268,430	9,012,928
Effect of exchange rate changes on cash	110,287	176,578
Net (decrease) increase in cash and cash equivalents	(680,327)	2,570,571
Cash and cash equivalents:		
Beginning of period	24,848,227	15,822,495
End of period	$24,167,900	$18,393,066
Supplemental disclosure of cash flow information:		
Income taxes paid	$1,429,000	$—

See notes to unaudited condensed consolidated financial statements

KOPIN CORPORATION

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION

The condensed consolidated financial statements of Kopin Corporation (the Company) as of March 31, 2018 and for the three month periods ended March 31, 2018 and April 1, 2017 are unaudited and include all adjustments which, in the opinion of management, are necessary to present fairly the results of operations for the periods then ended. These condensed consolidated financial statements should be read in conjunction with the Company’s financial statements and notes thereto, included in the Company’s Annual Report on Form 10-K for the year ended December 30, 2017. The results of the Company's operations for any interim period are not necessarily indicative of the results of the Company's operations for any other interim period or for a full fiscal year. The Company reclassified certain prior period amounts to conform to the current period presentation.

2. ACCOUNTING STANDARDS

Recently Issued Accounting Pronouncements

Leases

In February 2016, the FASB issued Accounting Standards Update ("ASU") No. 2016-02 (Topic 842) Leases, which requires lessees to recognize a right-of-use asset and lease liability for most lease arrangements. The new standard is effective for fiscal years beginning after December 15, 2018, with early adoption permitted, and must be adopted using the modified retrospective approach. The Company intends to adopt the standard on the effective date of December 30, 2018. The Company is currently evaluating the potential changes from this ASU to its future financial reporting and disclosures and designing and implementing related processes and controls.

Recently Adopted Accounting Pronouncements

Recognition and Measurement of Financial Assets and Liabilities

The Company adopted ASU No. 2016-01 and the related amendments on December 31, 2017 (the first day of the Company's fiscal year 2018). This standard amends various aspects of the recognition, measurement, presentation, and disclosure of financial instruments. The Company adopted the measurement alternative for equity investments without readily determinable fair values (often referred to as cost method investments) on a prospective basis. As a result, these investments will be revalued upon occurrence of an observable price change for similar investments and for impairments. The Company expects that the adoption of this guidance may have a material effect on its financial statements on an ongoing basis.

Revenue from Contracts with Customers

The Company adopted ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606) effective December 31, 2017 and applied the modified retrospective method. The Company recognized the cumulative effect of initially applying the new revenue standard as an adjustment to the opening balance of retained earnings. The comparative information has not been restated and continues to be reported under the accounting standards in effect for those periods. The Company expects the impact of the adoption of the new standard to be material to the Company's results of operations on an ongoing basis.

Significant Accounting Policies Update

The Company's significant accounting policies are detailed in "Note 1: Summary of Significant Accounting Policies" of our Annual Report on Form 10-K for the year ended December 30, 2017. Significant changes to the Company's accounting policies as a result of adopting Topic 606 are discussed below.

Revenue Recognition

The vast majority of our revenues are from orders received from our customers for the purchase of wearable technology components which can be integrated to create headset systems. We also have development contracts for the design, manufacture and modification of products for the U.S. government or a prime contractor for the U.S. government (“U.S. government”) or for a customer that sells into the industrial or consumer markets. The Company's contracts with the U.S. government are typically subject to the Federal Acquisition Regulations (“FAR”) and are priced based on estimated or actual costs of producing goods. The FAR provides guidance on the types of costs that are allowable in establishing prices for goods provided under U.S. government contracts. The pricing for non-U.S. government contracts is based on the specific negotiations with each customer.

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Our fixed-price contracts with the U.S. government may result in revenue recognized in excess of amounts actually billed. We present the in excess of revenues over amounts actually billed as Contract assets on the balance sheet. Amounts billed and due from our customers are classified as receivables on the balance sheet. In some instances, the U.S. government retains a small portion of the contract price until completion of the contract. The portion of the payments retained until final contract settlement is not considered a significant financing component because the intent is to protect the customer. For contracts with the U.S. government, we typically receive interim payments either as work progresses, we achieve certain milestones or based on a schedule in the contract. We recognize a liability for these advance payments in excess of revenue recognized and present it as billings in excess of revenue recognized on the balance sheet. The advanced payment typically is not considered a significant financing component because it is used to meet working capital demands that can be higher in the early stages of a contract and to protect us from the other party failing to adequately complete some or all of its obligations under the contract. For industrial and consumer purchase orders, we typically receive payments within 30 to 60 days of shipments of the product, although for some purchase orders, we may require an advanced payment prior to shipment of the product.

To determine the proper revenue recognition method for complex contracts with the same customer, we evaluate whether two or more contracts should be combined and accounted for as one single contract and whether the combined or single contract should be accounted for as more than one performance obligation. This evaluation requires significant judgment and the decision to combine a group of contracts or separate the combined or single contract into multiple performance obligations could change the amount of revenue and profit recorded in a given period. For most of our development contracts and contracts with the U.S government, the customer contracts with us to provide a significant service of integrating a set of components into a single unit. Hence, the entire contract is accounted for as one performance obligation. Less common, however, we may promise to provide distinct goods or services within a contract in which case we separate the contract into more than one performance obligation. If a contract is separated into more than one performance obligation, we allocate the total transaction price to each performance obligation in an amount based on the estimated relative standalone selling prices of the promised goods or services underlying each performance obligation. In cases where we sell standard products, the observable standalone sales are used to determine the standalone selling price.

The Company recognizes revenue from a contract when it has approval and commitment from both parties, the rights of the parties are identified, payment terms are identified, the contract has commercial substance and collectability of consideration is probable. For certain contracts that meet the foregoing requirements, primarily international direct commercial and military sale contracts, we recognize revenue once we have obtained all regulatory approvals.

Commencing in 2018 for certain contracts with the U.S. government, the Company recognizes revenue over time as we perform because of continuous transfer of control to the customer and the lack of an alternative use for the product. The continuous transfer of control to the customer is supported by liability clauses in the contract that allow the U.S. government to unilaterally terminate the contract for convenience, pay us for costs incurred plus a reasonable profit and take control of any work in process. For contracts with commercial customers while the contract may have similar liability clause our products historically have an alternative use and thus, revenue is recognized at a point in time.

In situations where control transfers over time, revenue is recognized based on the extent of progress towards completion of the performance obligation. We generally use the cost-to-cost approach to measure the extent of progress towards completion of the performance obligation for our contracts because we believe it best depicts the transfer of assets to the customer which occurs as we incur costs on our contracts. Under the cost-to-cost measure approach, the extent of progress towards completion is measured based on the ratio of costs incurred to date to the total estimated costs at completion of the performance obligation. Revenues are recorded proportionally as costs are incurred.

Accounting for design, development and production contracts requires judgment relative to assessing risks, estimating contract revenues and costs, and making assumptions for schedule and technical issues. Due to the size and nature of the work required to be performed on many of our contracts, the estimation of total revenue and cost at completion is complicated and subject to many variables. Contract costs include material, labor and subcontracting costs, as well as an allocation of indirect costs. We have to make assumptions regarding the number of labor hours required to complete a task, the complexity of the work to be performed, the availability and cost of materials, and performance by our subcontractors. For contract change orders, claims or similar items, we apply judgment in estimating the amounts and assessing the potential for realization. These amounts are only included in contract value when they can be reliably estimated and realization is considered probable. If our estimate of total contract costs or our determination of whether the customer agrees that a milestone is achieved is incorrect, our revenue could be overstated or understated and the profits or loss reported could be wrong.

For our commercial customers, the Company's revenue is recognized when obligations under the terms of a contract with our customer is satisfied; generally this occurs with the transfer of control of the Company's products or services. Revenue is recorded as the amount of consideration we expect to receive in exchange for transferring goods or providing services.

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Provisions for product returns and allowances are recorded in the same period as the related revenues. We analyze historical returns, current economic trends and changes in customer demand and acceptance of product when evaluating the adequacy of sales returns and other allowances. Certain product sales are made to distributors under agreements allowing for a limited right of return on unsold products. Sales to distributors are primarily made for sales to the distributors' customers and not for stocking of inventory. We delay revenue recognition for our estimate of distributor claims of right of return on unsold products based upon our historical experience with our products and specific analysis of amounts subject to return based upon discussions with our distributors or their customers. Sales, value add and other taxes we collect concurrent with revenue-producing activities are excluded from revenue.

The rights and benefits to the Company's intellectual property are conveyed to certain customers through technology license agreements. These agreements may include other performance obligations including the sale of product to the customer. When the license is distinct from other obligations in the agreement, the Company treats the license and other performance obligations as separate performance obligations. Accordingly, the license is recognized at a point in time or over time based on the standalone selling price. The sale of materials are recognized at a point in time, which occurs with the transfer of control of the Company's products or services. In certain instances, the Company is entitled to sales-based royalties under license agreements. These sales-based royalties are recognized when they are earned.

The cumulative effect of the changes made to the Company's consolidated December 31, 2017 balance sheet for the adoption of ASU 2014-09, Revenue from Contracts with Customers (Topic 606) was as follows:

Balance Sheet	Balance at December 30, 2017	Adjustments due to ASC 606	Balance at December 31, 2017
Assets			
Contract assets and unbilled receivables	$704,863	$2,850,274	$3,555,137
Inventory	5,080,797	(1,082,629)	3,998,168
Other assets	3,842,068	400,000	4,242,068
Liabilities			
Contract liabilities and billings in excess of revenue earned	896,479	(891,737)	4,742
Stockholders’ equity			
Accumulated Deficit	$(240,121,901)	$3,059,382	$(237,062,519)

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In accordance with the new revenue standard requirements, the impact of adoption on the Company's condensed consolidated statement of operations and condensed balance sheets was as follows:

	For the period ended March 31, 2018		
Statement of Operations	As Reported	Balances Without Adoption of ASC 606	Effect of Change Higher/(Lower)
Net product revenues	$5,044,809	$6,505,343	$ (1,460,534)
Research and development revenues	608,811	695,355	(86,544)
Cost of product revenues	4,062,191	5,069,765	(1,007,574)
Net loss attributable to the controlling interest	$(5,536,278)	$(4,996,773)	$ (539,505)

	For the period ended March 31, 2018		
Balance Sheet	As Reported	Balances Without Adoption of ASC 606	Effect of Change Higher/(Lower)
Assets			
Contract assets and unbilled receivables	$2,479,062	$1,089,322	$ 1,389,740
Inventory	3,773,305	3,848,359	(75,054)
Other assets	4,194,219	3,794,219	400,000
Liabilities			
Contract liabilities and billings in excess of revenue earned	384,073	1,189,266	(805,193)
Stockholders' equity			
Accumulated deficit	$(242,598,797)	$(245,082,132)	$ 2,483,335

See Note 11. Segments and Disaggregation of Revenue for additional information regarding the disaggregation of the Company's revenue by major source and the Company's updated accounting policy for revenue recognition.

Contract Assets

Contract assets include unbilled amounts typically resulting from sales under contracts when the cost-to-cost method of revenue recognition is utilized and revenue recognized exceeds the amount billed to the customer, and right to payment is not just subject to the passage of time. Amounts may not exceed their net realizable value. Contract assets are generally classified as current. The Company classifies the noncurrent portion of contract assets under other assets in its condensed consolidated balance sheets.

Contract Liabilities

Contract liabilities consist of advance payments and billings in excess of cost incurred and deferred revenue.

Remaining Performance Obligations

Remaining performance obligations represent the transaction price of firm orders for which work has not been performed and excludes unexercised contract options and potential orders under ordering-type contracts (e.g., indefinite-delivery, indefinite-quantity ("IDIQ")). As of March 31, 2018, the aggregate amount of the transaction price allocated to remaining performance obligations was $2.7 million. The Company expects to recognize revenue on the remaining performance obligations over the next 12 months.

3. CASH AND CASH EQUIVALENTS AND MARKETABLE SECURITIES

The Company considers all highly liquid, short-term debt instruments with original maturities of three months or less to be cash equivalents.

Marketable debt securities consist primarily of commercial paper, medium-term corporate notes, and U.S. government and agency backed securities. The Company classifies these marketable debt securities as available-for-sale at fair value in “Marketable debt securities, at fair value”. The Company records the amortization of premium and accretion of discounts on marketable debt securities in the results of operations.

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The Company uses the specific identification method as a basis for determining cost and calculating realized gains and losses with respect to marketable debt securities. The gross gains and losses realized related to sales and maturities of marketable debt securities were not material during the three months ended March 31, 2018 and the year ended December 30, 2017.

Investments in available-for-sale marketable debt securities are as follows at March 31, 2018 and December 30, 2017

	Amortized Cost		Unrealized Losses		Fair Value	
	2018	2017	2018	2017	2018	2017
U.S. government and agency backed securities	$29,821,596	$35,014,593	$(403,318)	$(288,782)	$29,418,278	$34,725,811
Corporate debt	7,270,853	8,988,608	(15,426)	(7,702)	7,255,427	8,980,906
Certificates of deposit	200,000	201,000	(110)	(260)	199,890	200,740
Total	$37,292,449	$44,204,201	$(418,854)	$(296,744)	$36,873,595	$43,907,457

The contractual maturity of the Company's marketable debt securities is as follows at March 31, 2018:

	Less than One year	One to Five years	Greater than Five years	Total
U.S. government and agency backed securities	$16,970,998	$11,498,340	$948,940	$29,418,278
Corporate debt	1,041,720	6,213,707	—	7,255,427
Certificates of deposit	199,890	—	—	199,890
Total	$18,212,608	$17,712,047		