AtriCure, Inc.
Form 10-Q
August 05, 2016
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 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, 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 000-51470

AtriCure, Inc.

(Exact name of Registrant as specified in its charter)

Delaware	34-1940305
(State or other jurisdiction	(IRS Employer

of incorporation) Identification No.)

7555 Innovation Way

Mason, OH 45040

(Address of principal executive offices)

(513) 755-4100

(Registrant's telephone number, including area code)

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

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 (Do not check if a smaller reporting company)	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

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

Class	Outstanding at August 3, 2016
Common Stock, $.001 par value	33,202,924

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

ATRICURE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(In Thousands, Except Per Share Amounts)

(Unaudited)

	June 30, 2016	December 31, 2015
Assets		
Current assets:		
Cash and cash equivalents	$ 19,917	$ 23,764
Short-term investments	22,510	10,814
Accounts receivable, less allowance for doubtful accounts of $75 and $136, respectively	21,354	19,409
Inventories	19,311	17,659
Other current assets	3,373	3,106
Total current assets	86,465	74,752
Property and equipment, net	30,902	31,279
Long-term investments	5,525	7,706
Intangible assets, net	52,953	53,775
Goodwill	105,257	105,257
Other noncurrent assets	411	323
Total Assets	$ 281,513	$ 273,092
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$ 11,926	$ 12,744
Accrued liabilities	12,790	18,394
Other current liabilities and current maturities of capital leases	473	450
Total current liabilities	25,189	31,588
Capital leases	13,504	13,710
Long-term debt	24,969	—
Other noncurrent liabilities	40,851	41,109
Total Liabilities	104,513	86,407
Commitments and contingencies (Note 7)		

Stockholders’ Equity:		
Common stock, $0.001 par value, 90,000 shares authorized and 33,203 and 32,274 issued and		
outstanding, respectively	33	32
Additional paid-in capital	361,023	352,900
Accumulated other comprehensive loss	(490)	(611)
Accumulated deficit	(183,566)	(165,636)
Total Stockholders’ Equity	177,000	186,685
Total Liabilities and Stockholders’ Equity	$ 281,513	$ 273,092

See accompanying notes to condensed consolidated financial statements.

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ATRICURE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS

(In Thousands, Except Per Share Amounts)

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Revenue	$ 39,672	$ 32,583	$ 75,612	$ 62,469
Cost of revenue	10,854	9,466	20,880	17,617
Gross profit	28,818	23,117	54,732	44,852
Operating expenses:				
Research and development expenses	9,124	5,862	17,687	11,471
Selling, general and administrative expenses	27,432	22,074	54,202	43,344
Total operating expenses	36,556	27,936	71,889	54,815
Loss from operations	(7,738)	(4,819)	(17,157)	(9,963)
Other income (expense):				
Interest expense	(477)	(17)	(736)	(35)
Interest income	60	43	99	86
Other	(34)	(90)	(114)	(231)
Loss before income tax expense	(8,189)	(4,883)	(17,908)	(10,143)
Income tax expense	17	8	22	14
Net loss	$ (8,206)	$ (4,891)	$ (17,930)	$ (10,157)
Basic and diluted net loss per share	$ (0.26)	$ (0.18)	$ (0.57)	$ (0.37)
Weighted average shares outstanding—basic and diluted	31,575	27,304	31,466	27,187
Comprehensive loss:				
Unrealized gains on investments	$ 13	$ 2	$ 54	$ 39
Foreign currency translation adjustment	(219)	253	67	(234)
Other comprehensive income (loss)	(206)	255	121	(195)
Net loss	(8,206)	(4,891)	(17,930)	(10,157)
Comprehensive loss	$ (8,412)	$ (4,636)	$ (17,809)	$ (10,352)

See accompanying notes to condensed consolidated financial statements.

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ATRICURE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In Thousands)

(Unaudited)

	Six Months Ended June 30,	
	2016	2015
Cash flows from operating activities:		
Net loss	$ (17,930)	$ (10,157)
Adjustments to reconcile net loss to net cash used in operating activities:		
Share-based compensation expense	5,869	4,141
Depreciation	3,678	2,087
Amortization of intangible assets	822	606
Amortization of deferred financing costs	86	31
Loss on disposal of property and equipment	117	63
Realized (gain) loss from foreign exchange on intercompany transactions	(15)	302
Amortization/accretion on investments	74	339
Change in allowance for doubtful accounts	(49)	117
Changes in operating assets and liabilities:		
Accounts receivable	(1,897)	(468)
Inventories	(1,595)	(1,977)
Other current assets	(236)	(538)
Accounts payable	131	1,128
Accrued liabilities	(5,673)	(2,196)
Other noncurrent assets and liabilities	(338)	128
Net cash used in operating activities	(16,956)	(6,394)
Cash flows from investing activities:		
Purchases of available-for-sale securities	(21,940)	(10,302)
Sales and maturities of available-for-sale securities	12,404	20,460
Purchases of property and equipment	(4,341)	(4,077)
Increases in property under build-to-suit obligation	—	(4,806)
Net cash (used in) provided by investing activities	(13,877)	1,275
Cash flows from financing activities:		
Proceeds from debt borrowings	25,000	—
Payments on capital leases	(218)	(25)
Increases in build-to-suit obligation	—	4,806
Payment of debt fees	(120)	(62)

Proceeds from stock option exercises	2,301	1,854
Shares repurchased for payment of taxes on stock awards	(1,033)	(572)
Proceeds from issuance of common stock under employee stock purchase plan	987	906
Net cash provided by financing activities	26,917	6,907
Effect of exchange rate changes on cash and cash equivalents	69	(185)
Net (decrease) increase in cash and cash equivalents	(3,847)	1,603
Cash and cash equivalents—beginning of period	23,764	28,384
Cash and cash equivalents—end of period	$ 19,917	$ 29,987
Supplemental cash flow information:		
Cash paid for interest	$ 577	$ 3
Cash paid for income taxes	—	20
Non-cash investing and financing activities:		
Accrued purchases of property and equipment	306	1,652
Assets acquired through capital lease	43	36
Capital lease asset early termination	9	—

See accompanying notes to condensed consolidated financial statements.

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ATRICURE, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

1. DESCRIPTION OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of the Business—AtriCure, Inc. was incorporated in the State of Delaware on October 31, 2000. The "Company" or "AtriCure" consists of AtriCure, Inc. and its wholly-owned subsidiaries. The Company is a leading atrial fibrillation (Afib) solutions partner providing innovative products, professional education and support for clinical science to reduce the economic and social burden of atrial fibrillation. The Company sells its products to medical centers globally through a direct sales force and distributors.

Basis of Presentation—The accompanying interim financial statements have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission (SEC). The accompanying interim financial statements are unaudited, but in the opinion of the Company's management, contain all of the normal, recurring adjustments considered necessary to present fairly the financial position, results of operations and cash flows for the periods presented in conformity with accounting principles generally accepted in the United States of America (GAAP) applicable to interim periods. Certain information and footnote disclosures normally included in annual financial statements prepared in accordance with GAAP have been omitted or condensed. The Company believes the disclosures herein are adequate to make the information presented not misleading. Results of operations are not necessarily indicative of the results expected for the full fiscal year or for any future period.

The accompanying Condensed Consolidated Financial Statements should be read in conjunction with the audited financial statements of the Company included in the Company's Annual Report on Form 10-K for the year ended December 31, 2015 filed with the SEC.

Principles of Consolidation—The Condensed Consolidated Financial Statements include the accounts of the Company, AtriCure, LLC, Endoscopic Technologies, LLC and nContact Surgical, LLC, the Company's wholly-owned subsidiaries, all organized in the State of Delaware, AtriCure Europe B.V. (AtriCure Europe), the Company's wholly-owned subsidiary incorporated in the Netherlands and AtriCure Hong Kong Limited, the Company's wholly-owned subsidiary incorporated in Hong Kong. All intercompany accounts and transactions have been eliminated in consolidation.

Cash and Cash Equivalents—The Company considers highly liquid investments with maturities of three months or less at the date of acquisition as cash equivalents in the accompanying Condensed Consolidated Financial Statements.

Investments—The Company places its investments primarily in U.S. Government agencies and securities, corporate bonds and commercial paper. The Company classifies all investments as available-for-sale. Investments with maturities of less than one year are classified as short-term investments. Investments are recorded at fair value, with unrealized gains and losses recorded as accumulated other comprehensive income (loss). The Company recognizes gains and losses when these securities are sold using the specific identification method and includes them in interest income or expense in the Condensed Consolidated Statements of Operations and Comprehensive Loss.

Revenue Recognition—The Company accounts for revenue in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 605, "Revenue Recognition" (ASC 605). The Company recognizes revenue when all of the following criteria are met: (i) there is persuasive evidence that an arrangement exists; (ii) delivery of the products and/or services has occurred; (iii) the selling price is fixed or determinable; and (iv) collectability is reasonably assured.

Pursuant to the Company's standard terms of sale, revenue is recognized when title to the goods and risk of loss transfers to customers and there are no remaining obligations that will affect the customers' final acceptance of the sale. Generally, the Company's standard terms of sale define the transfer of title and risk of loss to occur upon shipment to the respective customer. The Company does not normally maintain any post-shipping obligations to the recipients of the products. No installation, calibration or testing of products is performed by the Company subsequent to shipment to the customer in order to render it operational.

Revenue includes shipping and handling revenue of $329 and $271 for the three months ended June 30, 2016 and 2015, and $625 and $518 for the six months ended June 30, 2016 and 2015, respectively. Cost of freight for shipments made to customers is included in cost of revenue. Sales and other value-added taxes collected from customers and remitted to governmental authorities are excluded from revenue. The Company sells its products primarily through a direct sales force, with certain international markets sold through distributors. Terms of sale are generally consistent for both end-users and distributors except that payment terms are generally net 30 days for end-users and net 60 days for distributors with limited exceptions.

Sales Returns and Allowances—The Company maintains a provision for sales returns and allowances to account for potential returns of defective or damaged products, products shipped in error and invoice adjustments. The Company estimates such provision on a quarterly basis based primarily on specific identification, in addition to estimating a general reserve based on historical experience. Increases to the provision result in a reduction of revenue. The provision is included in accrued liabilities in the Condensed Consolidated Balance Sheets.

ATRICURE, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

Allowance for Doubtful Accounts Receivable—The Company evaluates the collectability of accounts receivable to determine the appropriate reserve for doubtful accounts. In determining the amount of the reserve, the Company considers aging of account balances, historical credit losses, customer-specific information and other relevant factors. An increase to the allowance for doubtful accounts results in a corresponding increase in selling, general and administrative expense. The Company reviews accounts receivable and adjusts the allowance based on current circumstances and charges off uncollectible receivables against the allowance when all attempts to collect the receivable have failed. The Company's history of write-offs against the allowance has not been significant.

Inventories—Inventories are stated at the lower of cost or market using approximate costs based on the first-in, first-out cost method (FIFO). Inventories consist of raw materials, work in process and finished goods. The Company's industry is characterized by rapid product development and frequent new product introductions. Uncertain timing of product approvals, variability in product launch strategies and variation in product utilization all impact excess and obsolete inventory. An inventory allowance based on product usage is estimated and recorded quarterly for excess, slow moving and obsolete inventory, as well as inventory with a carrying value in excess of its net realizable value. An increase to the inventory reserve allowance results in a corresponding increase in cost of revenue. Write-offs are recorded when a product is destroyed. The Company's history of write-offs against the reserve has not been significant.

Inventories consist of the following:

	June 30, 2016	December 31, 2015
Raw materials	$ 5,581	$ 6,159
Work in process	1,418	974
Finished goods	12,312	10,526
Inventories	$ 19,311	$ 17,659

Property and Equipment—Property and equipment is stated at cost less accumulated depreciation. Depreciation is computed using the straight-line method of depreciation for financial reporting purposes and is applied over the estimated useful lives of the assets. The estimated useful life by major asset category is the following: generators and other capital equipment, machinery, equipment and vehicles is three to seven years, computer and other office equipment is three years, furniture and fixtures is three to seven years and leasehold improvements and equipment under capital leases are the shorter of their useful life or remaining lease term. The Company reassesses the useful lives of property and equipment annually, and assets are retired if they are no longer in service. Maintenance and repair costs are expensed as incurred.

Generators and other capital equipment (such as the Company's switchbox units and cryosurgical consoles) are placed with direct customers that use the Company's disposable products. Depreciation of such assets is included in cost of revenue. The estimated useful lives of this equipment are based on anticipated usage by customers and the timing and impact of expected new technology rollouts by the Company. To the extent the Company experiences changes in the usage of this equipment or introduces new technologies, the estimated useful lives of this equipment may change in a future period. Depreciation related to these generators was $879 and $673 for the three months ended June 30, 2016 and 2015, respectively, and $1,715 and $1,293 for the six months ended June 30, 2016 and 2015, respectively. As of June 30, 2016 and December 31, 2015, the net carrying amount of loaned equipment included in net property and equipment in the Condensed Consolidated Balance Sheets was $5,454 and $5,447, respectively.

The Company reviews property and equipment for impairment using its best estimates based on reasonable and supportable assumptions and projections.

Intangible Assets—Intangible assets with determinable useful lives are amortized on a straight-line basis over the estimated periods benefited.

Included in intangible assets is In Process Research and Development (IPR&D). The Company defines IPR&D as the value of acquired technology which has not yet reached technological feasibility. The primary basis for determining the technological feasibility is obtaining specific regulatory approvals. The estimated fair value of IPR&D acquired in a business combination is capitalized as an indefinite-lived intangible asset until completion or abandonment of the IPR&D project. Upon completion of the development project, the IPR&D is amortized over its estimated useful life. If the IPR&D project is abandoned, the related IPR&D asset is written off. The estimated fair value of IPR&D was determined using an income approach model and represents an estimate of the fair value of the PMA approval that could result from the CONVERGE IDE clinical trial.

The Company reviews intangible assets for impairment using its best estimates based on reasonable and supportable assumptions and projections.

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ATRICURE, INC. AND SUBSIDIARIES

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(In thousands, except per share amounts)

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Goodwill—Goodwill represents the excess of purchase price over the fair value of the net assets acquired in business combinations. The Company tests goodwill for impairment annually on November 30, or more often if impairment indicators are present. The Company's goodwill is accounted for in a single reporting unit representing the Company as a whole.

Other Noncurrent Liabilities—Other noncurrent liabilities include contingent consideration recorded in business combinations, as well as long-term deferred revenues and other contractual obligations.

Other Income—Other income consists primarily of foreign currency transaction gains and losses. The Company recorded net foreign currency transaction losses of $35 and $46 for the three months ended June 30, 2016 and 2015, respectively, and $115 and $209 for the six months ended June 30, 2016 and 2015, respectively, in connection with settlements of its intercompany balance with AtriCure Europe and sales invoices transacted in British Pounds.

Taxes—Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities from a change in tax rates is recognized in the period that includes the enactment date.

The Company's estimate of the valuation allowance for deferred tax assets requires it to make significant estimates and judgments about its future operating results. Deferred tax assets are reduced by valuation allowances if, based on the consideration of all available evidence, it is more-likely-than-not that some portion of the deferred tax asset will not be realized. Significant weight is given to evidence that can be objectively verified. The Company evaluates deferred tax assets on a quarterly basis to determine if valuation allowances are required by considering all available evidence. Deferred tax assets are realized by having sufficient future taxable income to allow the related tax benefits to reduce taxes otherwise payable. The sources of taxable income that may be available to realize the benefit of deferred tax assets are future reversals of existing taxable temporary differences, future taxable income, exclusive of reversing temporary differences and carryforwards, taxable income in carry-back years and tax planning strategies that are both prudent and feasible. In evaluating whether to record a valuation allowance, the applicable accounting standards deem that the existence of cumulative losses in recent years is a significant piece of objectively verifiable negative evidence that must be overcome by objectively verifiable positive evidence to avoid the need to record a valuation allowance. The Company has recorded a full valuation allowance against its net deferred tax assets as it is more likely than not that the benefit of the deferred tax assets will not be recognized in future periods.

A provision of The Patient Protection and Affordable Care Act enacted in 2010, as amended (Patient Act), required manufacturers of medical devices to pay an excise tax on all U.S. medical device sales. In December 2015, the U.S. government approved the suspension of the excise tax on medical device sales beginning January 1, 2016 through December 31, 2017. The Company's expense related to the medical device excise tax, which was recorded in cost of revenue, was $0 and $149 for the three months ended June 30, 2016 and 2015, respectively, and $0 and $304 for the six months ended June 30, 2016 and 2015, respectively.

Net Loss Per Share—Basic and diluted net loss per share is computed in accordance with FASB ASC 260, “Earnings Per Share” (ASC 260) by dividing the net loss by the weighted average number of common shares outstanding during the period. Since the Company has experienced net losses for all periods presented, net loss per share excludes the effect of 4,471 and 4,290 stock options and restricted stock shares as of June 30, 2016 and 2015, respectively, because they are anti-dilutive. Therefore the number of shares calculated for basic net loss per share is also used for the diluted net loss per share calculation.

Comprehensive Loss and Accumulated Other Comprehensive Loss—In addition to net losses, the comprehensive loss includes foreign currency translation adjustments and unrealized gains and losses on investments.

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ATRICURE, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

Accumulated other comprehensive income (loss) consisted of the following:

	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015
Total accumulated other comprehensive loss at beginning of period	$ (284)	$ (798)	$ (611)	$ (348)
Unrealized Gains on Investments				
Balance at beginning of period	$ 2	$ (17)	$ (39)	$ (54)
Other comprehensive income (loss) before reclassifications	13	2	54	39
Amounts reclassified from accumulated other comprehensive income to other income on the statement of operations	—	—	—	—
Balance at end of period	$ 15	$ (15)	$ 15	$ (15)
Foreign Currency Translation Adjustment				
Balance at beginning of period	$ (286)	$ (781)	$ (572)	$ (294)
Other comprehensive income (loss) before reclassifications	(229)	392	52	68
Amounts reclassified from accumulated other comprehensive income to other income on the statement of operations	10	(139)	15	(302)
Balance at end of period	$ (505)	$ (528)	$ (505)	$ (528)
Total accumulated other comprehensive loss at end of period	$ (490)	$ (543)	$ (490)	$ (543)

Research and Development—Research and development costs are expensed as incurred. These costs include compensation and other internal and external costs associated with the development and research related to new and existing products or concepts, preclinical studies, clinical trials, healthcare compliance and regulatory affairs.

Advertising Costs— The Company expenses advertising costs as incurred. Advertising costs were not significant during the three and six months ended June 30, 2016 and 2015.

Share-Based Compensation—The Company follows FASB ASC 718, “Compensation-Stock Compensation” (ASC 718) to record share-based compensation for all employee share-based payment awards, including stock options, restricted stock and stock purchases related to an employee stock purchase plan, based on estimated fair values. The Company's share-based compensation expense recognized under ASC 718 for the three months ended June 30, 2016 and 2015 was $3,027 and $2,417, respectively, and $5,869 and $4,141, respectively, for the six months ended June 30, 2016 and 2015, on a before and after tax basis.

ASC 718 requires companies to estimate the fair value of share-based payment awards on the date of grant using an option-pricing model. The value of the portion of the award that is ultimately expected to vest is recognized as expense over the requisite service periods in the Company's Condensed Consolidated Statement of Operations and Comprehensive Loss. The expense has been reduced for estimated forfeitures. ASC 718 requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates.

The Company estimates the fair value of time-based options on the date of grant using the Black-Scholes option-pricing model (Black-Scholes model). The Company's determination of fair value of share-based payment awards on the date of grant using an option-pricing model is affected by the Company's stock price, as well as assumptions regarding a number of subjective variables. These variables include but are not limited to the Company's expected stock price volatility over the term of the awards and actual and projected employee stock option exercise behaviors. The fair value of market-based performance option grants is estimated at the date of grant using a Monte-Carlo simulation. The value of the portion of the award that is ultimately expected to vest is recognized as expense over the requisite service periods in the Consolidated Statement of Operations and Comprehensive Loss.

The Company estimates the fair value of restricted stock based upon the grant date closing market price of the Company's common stock. The Company's determination of fair value is affected by the Company's stock price as well as assumptions regarding the number of shares expected to be granted.

The Company also has an employee stock purchase plan (ESPP) which is available to all eligible employees as defined by the plan document. Under the ESPP, shares of the Company's common stock may be purchased at a discount. The Company estimates the number of shares to be purchased under the ESPP and records compensation expense based upon the fair value of the stock at the beginning of the purchase period using the Black-Scholes model.

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ATRICURE, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

Use of Estimates—The preparation of the financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and 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.

Fair Value Disclosures—The Company classifies and records cash and investments in U.S. government agencies and securities as Level 1 within the fair value hierarchy. Accounts receivable, short-term other assets, accounts payable and accrued liabilities are also classified as Level 1. The carrying amounts of these assets and liabilities approximate their fair value due to their relatively short-term nature. Cash equivalents and investments in corporate bonds and commercial paper are classified as Level 2 within the fair value hierarchy (see Note 3 – Fair Value for further information). The book value of the Company's fixed interest rate debt approximates its fair value as of June 30, 2016. Fixed interest rate debt fair value is determined by calculating the net present value of future debt payments and is classified as Level 2. Significant unobservable inputs with respect to the Level 3 fair value measurement of the contingent consideration liability is developed using Company data. When an input is changed, the corresponding valuation models are updated and the results are analyzed for reasonableness.

2. RECENT ACCOUNTING PRONOUNCEMENTS

In May 2014 the FASB issued a final standard on revenue from contracts with customers. The standard, issued as FASB ASU 2014-09, "Revenue from Contracts with Customers" (ASU 2014-09), outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance. In July 2015 the FASB decided to defer the effective date of ASU 2014-09 for entities reporting under U.S. GAAP from interim and annual reporting periods beginning after December 15, 2016 to interim and annual reporting periods beginning after December 15, 2017 and allow early adoption as of the original effective date. A full retrospective or modified retrospective approach may be taken to adopt the guidance in the ASU. FASB ASU 2016-08, "Revenue from Contracts with Customers (Topic 606): Principal Versus Agent Considerations (Reporting Revenue Gross Versus Net)", FASB ASU 2016-10, "Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing", and FASB ASU 2016-12, "Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients", have been issued in 2016 to further refine the guidance in ASU 2014-09. The Company is evaluating the impact of the provisions of the revenue-related ASUs on its consolidated financial position, results of operations and related disclosures.

In November 2015 the FASB issued ASU 2015-17, "Income Taxes (Topic 740), Balance Sheet Classification of Deferred Taxes" (ASU 2015-17), which requires companies to classify all deferred tax assets and liabilities as noncurrent on the balance sheet instead of separating deferred taxes into current and noncurrent amounts. Also, companies will no longer allocate valuation allowances between current and noncurrent deferred tax assets because those allowances also will be classified as noncurrent. ASU 2015-17 is effective for financial statements issued for annual periods beginning after December 15, 2016, and interim periods within those annual periods. Early adoption is permitted for financial statements that have not been issued. The Company has evaluated the impact of the provisions of ASU 2015-17 on its consolidated financial position and related disclosures and has determined that the new guidance does not have a material impact on its financial reporting.

In January 2016 the FASB issued ASU 2016-01, “Financial Instruments — Overall — Recognition and Measurement of Financial Assets and Financial Liabilities” (ASU 2016-01), which amends the guidance in U.S. GAAP on the classification and measurement of financial instruments. Although the ASU retains many current requirements, it significantly revises an entity’s accounting related to (1) the classification and measurement of investments in equity securities and (2) the presentation of certain fair value changes for financial liabilities measured at fair value. The ASU also amends certain disclosure requirements associated with the fair value of financial instruments. The new standard is effective for fiscal years and interim periods within those fiscal years beginning after December 15, 2017. The Company is evaluating the impact of ASU 2016-01 on its consolidated financial position and related disclosures.

In February 2016 the FASB issued ASU 2016-02, “Leases” (ASU 2016-02) which requires lessees to record most leases onto their balance sheet but recognize expenses on their income statement in a manner similar to today’s accounting. The guidance is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Entities are required to use a modified retrospective approach for leases that exist or are entered into after the beginning of the earliest comparative period in the financial statements. Full retrospective application is prohibited. The Company is evaluating the provisions of ASU 2016-02 to determine the impact on its consolidated financial position and related disclosures.

In March 2016 the FASB issued ASU 2016-09, “Improvements to Employee Share-Based Payment Accounting” (ASU 2016-09), which changes certain aspects of accounting for share-based payments to employees. The new guidance requires all income tax effects of awards to be recognized in the income statement when the awards vest or are settled. It also allows an employer to repurchase more of an employee's shares for tax withholding purposes without triggering liability accounting and to make a policy election to account for forfeitures as they occur rather than apply an estimate for expense recognition. ASU 2016-09 is effective for fiscal years beginning after December 15, 2016, and interim periods within those years. Early adoption is permitted, however, all of the guidance within the ASU must be adopted in the same period. The Company is evaluating the impact of ASU 2016-09 on its consolidated financial position, results of operations and related disclosures.

In June 2016 the FASB issued ASU 2016-13, "Financial Instruments—Credit Losses—Measurement of Credit Losses on Financial Instruments" (ASU 2016-13), which changes how entities will measure credit losses for most financial assets and certain other instruments that are not measured at fair value through net income. The standard replaces today's "incurred loss" approach with an "expected loss" model for instruments measured at amortized cost and requires entities to record allowances for available-for-sale debt securities rather than reduce the carrying amount, as they do today under the other-than-temporary impairment model. It also simplifies the accounting model for purchased credit-impaired debt securities and loans. ASU 2016-13 is effective for annual periods beginning after December 15, 2019, and interim periods therein. Early adoption is permitted for annual periods beginning after December 15, 2018, and interim periods therein. The Company is evaluating the impact of ASU 2016-13 on its consolidated financial position, results of operations and related disclosures.

3. FAIR VALUE

FASB ASC 820, "Fair Value Measurements and Disclosures" (ASC 820) defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value must maximize the use of observable inputs and minimize the use of unobservable inputs. The standard describes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value which are the following:

- Level 1—Quoted prices in active markets for identical assets or liabilities that the Company has the ability to access at the measurement date. An active market for the asset or liability is a market in which transactions for the asset or liability occur with sufficient frequency and volume to provide pricing information on an ongoing basis. The valuation under this approach does not entail a significant degree of judgment.
- Level 2—Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. The valuation technique for the Company's Level 2 assets is based on quoted market prices for similar assets from observable pricing sources at the reporting date.

- 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. Unobservable inputs shall be used to measure fair value to the extent that observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at the measurement date. The fair value of the Company’s contingent consideration liability was estimated on the acquisition date of nContact Surgical, Inc. (nContact) using Level 3 inputs.

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ATRICURE, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share amounts)

(Unaudited)

In accordance with ASC 820, the following table represents the Company's fair value hierarchy for its financial assets and liabilities measured at fair value on a recurring basis as of June 30, 2016:

Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs