BSD MEDICAL CORP
Form 10-Q
January 09, 2014

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

[Missing Graphic Reference]
FORM 10-Q

(Mark One)

ý Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended November 30, 2013

o Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from ___________ to __________

Commission File No. 001-32526

BSD Medical Corporation
(Exact Name of Registrant as Specified in Its Charter)

Delaware (State or other jurisdiction of incorporation or organization)	75-1590407 (I.R.S. Employer Identification No.)

2188 West 2200 South
Salt Lake City, Utah 84119
(Address of principal executive offices, including zip code)

(801) 972-5555
(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 ý No o

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 ý No o

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. (Check one):

Large accelerated filer o	Accelerated filer o
Non-accelerated filer o	Smaller reporting company ý

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No ý

As of January 8, 2014, there were 33,981,871 shares of the Registrant's common stock, $0.001 par value per share, outstanding.

BSD MEDICAL CORPORATION
FORM 10-Q

FOR THE QUARTER ENDED NOVEMBER 30, 2013

PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

BSD MEDICAL CORPORATION
Condensed Balance Sheets
(Unaudited)

ASSETS	November 30, 2013	August 31, 2013
Current assets:		
Cash and cash equivalents	$7,580,268	$9,450,528
Accounts receivable, net of allowance for doubtful accounts of $20,000	1,150,206	899,969
Related party trade accounts receivable	40,887	24,201
Inventories, net	2,630,414	2,445,770
Other current assets	160,954	200,028
Total current assets	11,562,729	13,020,496
Property and equipment, net	1,301,535	1,319,880
	$12,864,264	$14,340,376
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$511,873	$521,417
Accrued liabilities	416,040	573,880
Customer deposits	334,577	317,480
Deferred revenue – current portion	707,501	730,593
Total current liabilities	1,969,991	2,143,370
Deferred revenue – net of current portion	47,014	53,115
Total liabilities	2,017,005	2,196,485
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, $.001 par value; 10,000,000 shares authorized, no shares issued and outstanding	-	-
Common stock, $.001 par value, 80,000,000 shares authorized, 34,006,202 shares issued	34,007	34,007
Additional paid-in capital	57,955,285	57,739,056
Treasury stock, 24,331 shares at cost	(234)	(234)
Accumulated deficit	(47,141,799)	(45,628,938)
Total stockholders' equity	10,847,259	12,143,891
	$12,864,264	$14,340,376

See accompanying notes to condensed financial statements

BSD MEDICAL CORPORATION
Condensed Statements of Comprehensive Loss
(Unaudited)

	Three Months Ended November 30, 2013	Three Months Ended November 30, 2012
Revenues:		
Sales	$1,231,559	$517,614
Sales to related parties	16,686	70,271
Equipment rental	82,400	71,900
Total revenues	1,330,645	659,785
Cost of revenues:		
Cost of sales	628,711	408,870
Cost of related party sales	7,654	61,377
Cost of equipment rental	2,947	2,947
Total cost of revenues	639,312	473,194
Gross margin	691,333	186,591
Operating costs and expenses:		
Research and development	502,757	527,267
Selling, general and administrative	1,704,713	1,889,249
Total operating costs and expenses	2,207,470	2,416,516
Loss from operations	(1,516,137)	(2,229,925)
Other income (expense):		
Interest income	6,323	9,946
Other income (expense)	(3,047)	1,315
Total other income (expense)	3,276	11,261
Loss before income taxes	(1,512,861)	(2,218,664)
Income tax benefit	-	-
Net loss and comprehensive loss	$(1,512,861)	$(2,218,664)
Net loss per common share:		
Basic	$(0.04)	$(0.07)
Diluted	$(0.04)	$(0.07)

Weighted average number of shares outstanding:		
Basic	33,982,000	29,778,000
Diluted	33,982,000	29,778,000

See accompanying notes to condensed financial statements

BSD MEDICAL CORPORATION
Condensed Statements of Cash Flows
(Unaudited)

	Three Months Ended November 30, 2013	2012
Cash flows from operating activities:		
Net loss	$(1,512,861)	$(2,218,664)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	30,121	37,272
Stock-based compensation	216,229	289,912
Decrease (increase) in:		
Receivables	(266,923)	(170,244)
Inventories	(184,644)	59,899
Other current assets	39,074	(16,304)
Increase (decrease) in:		
Accounts payable	(9,544)	14,590
Accrued liabilities	(157,840)	34,756
Customer deposits	17,097	16,270
Deferred revenue	(29,193)	(3,318)
Net cash used in operating activities	(1,858,484)	(1,955,831)
Cash flows from investing activities:		
Purchase of property and equipment	(11,776)	(4,160)
Cash flows from financing activities	-	-
Net decrease in cash and cash equivalents	(1,870,260)	(1,959,991)
Cash and cash equivalents, beginning of period	9,450,528	11,102,508
Cash and cash equivalents, end of period	$7,580,268	$9,142,517

See accompanying notes to condensed financial statements

BSD MEDICAL CORPORATION
Notes to Condensed Financial Statements
(Unaudited)

Note 1. Basis of Presentation

The interim financial information of BSD Medical Corporation (the "Company") as of November 30, 2013 and for the three months ended November 30, 2013 and 2012 is unaudited, and the condensed balance sheet as of August 31, 2013 is derived from our audited financial statements. The accompanying unaudited condensed balance sheets as of November 30, 2013 and August 31, 2013 and the related unaudited condensed statements of comprehensive loss and of cash flows for the three months ended November 30, 2013 and 2012 have been prepared in accordance with U.S. generally accepted accounting principles for interim financial reporting and pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC"). The condensed financial statements do not include all of the information and notes required by U.S. generally accepted accounting principles for complete financial statements. These condensed financial statements should be read in conjunction with the notes thereto, and the financial statements and notes thereto included in our annual report on Form 10-K for the year ended August 31, 2013.

All adjustments (consisting only of normal recurring adjustments) necessary for the fair presentation of our financial position as of November 30, 2013 and August 31, 2013 and our results of operations and our cash flows for the three months ended November 30, 2013 and 2012 have been included. The results of operations for the three months ended November 30, 2013 may not be indicative of the results for our fiscal year ending August 31, 2014.

Certain amounts in the prior periods have been reclassified to conform to the current period presentation.

Note 2. Inventories

Inventories consisted of the following:

	November 30, 2013	August 31, 2013
Parts and supplies	$ 1,397,216	$ 1,353,614
Work-in-process	1,025,547	990,668
Finished goods	357,651	201,488
Reserve for obsolete inventory	(150,000)	(100,000)
Inventories, net	$ 2,630,414	$ 2,445,770

Note 3. Property and Equipment

Property and equipment consisted of the following:

	November 30, 2013	August 31, 2013
Equipment	$ 1,411,684	$ 1,401,811
Rental equipment	58,940	58,940
Furniture and fixtures	301,964	300,061
Building improvements	54,736	54,736
Building	956,000	956,000
Land	244,000	244,000
	3,027,324	3,015,548
Less accumulated depreciation	(1,725,789)	(1,695,668)
Property and equipment, net	$ 1,301,535	$ 1,319,880

Note 4. Stockholders' Equity

The Company has 10,000,000 authorized shares of $.001 par value preferred stock. As of November 30, 2013 and August 31, 2013, there were no shares of preferred stock outstanding. The Company also has 80,000,000 authorized shares of $.001 par value common stock.

Shelf Registration Statement

On September 28, 2012, we filed a universal shelf registration statement (Form S-3; file number 333-184164) with the SEC for the issuance of common stock, preferred stock, warrants, senior debt, subordinated debt and units up to an aggregate amount of $50.0 million. On October 11, 2012, the universal shelf registration statement was declared effective by the SEC. We may periodically offer one or more of these securities in amounts, prices and terms to be announced when and if the securities are offered. At the time any of the securities covered by the registration statement are offered for sale, a prospectus supplement will be prepared and filed with the SEC containing specific information about the terms of any such offering.

In April 2013, we completed an offering of 4,065,042 shares of our common stock and warrants to purchase a total of 3,048,782 shares of our common stock with certain institutional investors. The warrants became exercisable six months and one day following the closing date of the offering and will remain exercisable for five years thereafter at an exercise price of $1.65 per share. The offering was completed using our shelf registration statement, and net proceeds to us were approximately $4.6 million.

Warrants

A summary of the outstanding warrants issued in prior stock offerings as of November 30, 2013, and changes during the three months then ended, is as follows:	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contract Term (Years)
Outstanding at August 31, 2013	5,457,305	$ 2.93	
Issued	-	-	
Exercised	-	-	
Forfeited or expired	-	-	
Outstanding and exercisable at November 30, 2013	5,457,305	$ 2.93	3.71

Note 5. Net Loss Per Common Share

The computation of basic earnings per common share is based on the weighted average number of shares outstanding during each period. The computation of diluted earnings per common share is based on the weighted average number of shares outstanding during the period plus the weighted average common stock equivalents which would arise from the exercise of stock options and warrants outstanding using the treasury stock method and the average market price per share during the period. Common stock equivalents are not included in the diluted loss per share calculation when their effect is anti-dilutive.

No stock options or warrants are included in the computation of diluted weighted average number of shares for the three months ended November 30, 2013 and 2012 because the effect would be anti-dilutive. As of November 30, 2013, we had outstanding options and warrants to purchase a total of 9,459,544 shares of our common stock that could have a future dilutive effect on the calculation of earnings per share.

Note 6. Related Party Transactions

During the three months ended November 30, 2013 and 2012, we had sales of $16,686 and $70,271, respectively, to entities controlled by a significant stockholder and member of the Board of Directors. These related party transactions represent approximately 1% and 11% of total sales for each respective three-month period.

As of November 30, 2013 and August 31, 2013, receivables included $40,887 and $24,201, respectively, from these related parties. Also, included in deposits from our customers as of November 30, 2013 and August 31, 2013 was $159,980 towards the purchase of a hyperthermia system from this same related party.

Note 7. Stock-Based Compensation

We have both an employee and director stock incentive plan, which are described more fully in Note 10 in our 2013 Annual Report on Form 10-K. As of November 30, 2013, we had approximately 1,860,000 shares of common stock reserved for future issuance under the stock incentive plans.

Stock-based compensation cost is measured at the grant date based on the value of the award granted using the Black-Scholes option pricing model, and recognized over the period in which the award vests. For stock awards no longer expected to vest, any previously recognized stock compensation expense is reversed in the period of termination. The stock-based compensation expense has been allocated to the various categories of operating costs and expenses in a manner similar to the allocation of payroll expense as follows:

	Three Months Ended November 30, 2013	2012
Cost of sales	$ 15,650	$ 16,023
Research and development	46,448	50,285
Selling, general and administrative	154,131	223,604
Total	$ 216,229	$ 289,912

During the three months ended November 30, 2013, we granted employees a total of 20,000 stock options at exercise prices ranging from $1.30 to $1.34 per share, generally with one third vesting each year for the next three years. The estimated weighted average grant date fair value per share of these stock options was $0.69, and our weighted average assumptions used in the Black-Scholes valuation model to determine this estimated fair value are as follows:

Expected volatility	64.41%
Expected dividends	0%
Expected term	7.35 years
Risk-free interest rate	2.02%

Unrecognized stock-based compensation expense expected to be recognized over the estimated weighted-average amortization period of 1.08 years is approximately $1,371,000 as of November 30, 2013.

A summary of the time-based stock option awards as of November 30, 2013, and changes during the three months then ended, is as follows:

	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contract Term (Years)	Aggregate Intrinsic Value
Outstanding at August 31, 2013	4,212,573	$ 2.85		
Granted	20,000	1.33		
Exercised	-	-		
Forfeited or expired	(230,334)	3.12		
Outstanding at November 30, 2013	4,002,239	$ 2.83	6.73	$ 65,801
Exercisable at November 30, 2013	2,053,597	$ 3.72	4.78	$ 37,301

The aggregate intrinsic value in the preceding table represents the total pre-tax intrinsic value, based on our closing stock price of $1.39 as of November 30, 2013, which would have been received by the holders of in-the-money options had the option holders exercised their options as of that date.

Note 8. Supplemental Cash Flow Information

We paid no amounts for interest expense and income taxes during the three months ended November 30, 2013 and 2012.

During the three months ended November 30, 2013 and 2012, we had no non-cash financing and investing activities.

Note 9. Recent Accounting Pronouncements

No new accounting pronouncements were adopted during the quarter ended November 30, 2013 that had a material impact on our financial statements. No new accounting pronouncements were issued during the quarter ended November 30, 2013 and through the date of filing this report that we believe are applicable or would have a material impact on our financial statements.

Note 10. Subsequent Events

Subsequent to November 30, 2013, the Board of Directors of the Company approved the grant of 80,000 stock options to an employee, with an exercise price of $1.17 per share and with one third vesting each year for the next three years.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

This Management's Discussion and Analysis of Financial Condition and Results of Operations and other parts of this quarterly report on Form 10-Q contain forward-looking statements that involve risks and uncertainties. Forward-looking statements can also be identified by words such as "anticipates," "expects," "believes," "plans," "predicts," and similar terms. Forward-looking statements are not guarantees of future performance and our actual results may differ significantly from the results discussed in the forward-looking statements. Factors that might cause such differences include, but are not limited to, those discussed in the subsection entitled "Forward-Looking Statements" below. The following discussion should be read in conjunction with our financial statements and notes thereto included in this report. We assume no obligation to revise or update any forward-looking statements for any reason, except as required by law.

Overview

BSD Medical Corporation (the "Company" or "BSD") was originally incorporated under the laws of the State of Utah on March 17, 1978. On July 3, 1986, the Company was reincorporated in the State of Delaware.

We develop, manufacture, market and service systems to treat cancer and benign diseases using heat therapy delivered using focused radiofrequency ("RF") and microwave energy. Our business objectives are to commercialize our products for the treatment of cancer and to further expand our products to treat other diseases and medical conditions. Our product line for cancer therapy has been created to offer hospitals and clinics a complete solution for thermal treatment of cancer using microwave/RF systems, including both ablation and hyperthermia treatment systems. Studies have shown that both ablation and hyperthermia treatments kill cancer, but they have different clinical applications.

Our microwave ablation system is used to ablate (destroy) soft tissue with heat alone. Thermal ablation usually refers to heat treatments delivered at temperatures above 55°C for short periods of time. Thermal ablation is used to destroy local tumors using a short intense focus of heat on a specific area.

Our hyperthermia cancer treatment systems are used to treat cancer with heat (hyperthermia) while boosting the effectiveness of radiation for certain tumors through a number of biological mechanisms. Hyperthermia is usually used to increase the effectiveness of other therapies; e.g., radiation therapy and chemotherapy for the treatment of locally advanced cancers. Hyperthermia usually refers to treatments delivered at temperatures of 40-45°C for one hour.

Commercialization of our systems that are used to treat cancer is our most immediate business objective. Current and future cancer treatment sites for our systems may include cancers of the prostate, breast, head, neck, bladder, cervix, colon/rectum, ovaries, esophagus, liver, kidney, brain, bone, stomach and lung. Our cancer treatment systems have been used to treat thousands of patients throughout the world and have received many awards, including the Frost & Sullivan "Technology Innovation of the Year Award" for cancer therapy devices, which was awarded in 2005 for the development of the BSD-2000 Hyperthermia System.

Although we have not yet taken advantage of many of these market opportunities, we believe that our technology has application for a number of other medical purposes in addition to cancer.

We are experiencing growth in our operating revenues from our MicroThermX® Microwave Ablation System ("MicroThermX") line of products as a result of an exclusive, long-term, multi-million dollar distribution agreement with Terumo Europe NV (Terumo), a wholly owned subsidiary of Terumo Corporation. The agreement with Terumo, which we announced in April 2013, covers 100 countries in Europe, Western Asia, and Northern Africa. In addition, MicroThermX revenues and sales of disposable SynchroWave antennas have increased in the US market as well.

The number of hyperthermia systems sold varies from period to period and sales are impacted by several factors including negative regulatory, economic and other healthcare industry factors. We have experienced declining hyperthermia revenues from our distributor in Europe, a related party. We have entered into distribution agreements for our hyperthermia systems in China, South Korea and Taiwan. We anticipate that these distribution agreements will result in increased hyperthermia sales in the future; however, certain regulatory approvals must first be obtained in these countries before we will realize increased sales, and we cannot currently predict the outcome of these efforts.

We recognize revenues from the sale of our ablation and hyperthermia cancer treatment systems and related parts and accessories (collectively, product sales), the sale of disposable devices used with certain of our systems, from training, and from service support contracts and other miscellaneous revenues. We also recognize revenues from equipment rental, including fee-per-use rental income from our MicroThermX.

Our current corporate strategy includes the possibility of entering into additional collaborative arrangements with third parties to expand and improve the commercialization of all our products, including our hyperthermia systems. The recent signing of the master distribution agreement with Terumo for our MicroThermX line of products was a result of this strategy. Consistent with this strategy, we engaged Roth Capital Partners on June 1, 2013, to serve as our exclusive advisor with the goal to seek out, identify opportunities and, if possible, secure a transaction or transaction(s) relating to BSD's hyperthermia business, including, but not limited to, partnering or other collaborative agreements, a sale of assets and/or other strategic arrangements. There can be no assurance that the exploration of strategic alternatives will result in any agreements or transactions, or that, if completed, any agreements or transactions will be successful or on attractive terms.

Backlog

As of the date of the filing of this report, we had a total sales backlog of approximately $2,215,000.

Results of Operations

Fluctuation in Operating Results

Our results of operations have fluctuated in the past and may fluctuate in the future from year to year as well as from quarter to quarter. Revenue may fluctuate as a result of factors relating to the demand and market acceptance for our ablation and hyperthermia systems and related component parts and services, world-wide economic conditions, availability of financing for our customers, changes in the medical capital equipment market, changes in order mix and product order configurations, competition, regulatory developments, insurance reimbursement and other matters. Operating expenses may fluctuate as a result of the timing of sales and marketing activities, research and development, and general and administrative expenses associated with our potential growth. For these and other reasons described elsewhere, our results of operations for a particular period may not be indicative of operating results for any other period.

Revenues

We recognized revenue from the sale of our ablation and hyperthermia cancer treatment systems and related parts and accessories (collectively, product sales), the sale of disposable devices used with certain of our systems, from training, and from service support contracts and other miscellaneous revenues. We also recognized revenues from equipment rental, including our fee-per-use rental income from our MicroThermX.

Our revenues consisted of the following:

	Three Months Ended November 30, 2013	Three Months Ended November 30, 2012
Product sales	$ 804,400	$ 269,000
Disposable devices	361,760	225,775
Service contracts and other	82,085	93,110
	1,248,245	587,885
Equipment rental	82,400	71,900
Total	$ 1,330,645	$ 659,785

Total revenues in the three months ended November 30, 2013 increased $670,860, or 102%, compared to total revenues in the three months ended November 30, 2012. The growth in revenue during the first quarter of fiscal year 2014 resulted from both increased MicroThermX and hyperthermia sales.

During the third quarter of fiscal year 2013, we commenced shipping MicroThermX systems and SynchroWave antennas to Terumo Europe pursuant to an exclusive distribution agreement covering 100 countries in Europe, Western Asia, and Northern Africa. In addition, with the successful introduction of our fee-per-use rental program and accelerating sales of disposable SynchroWave antennas, our revenues from our MicroThermX family of products continue to grow.

During the three months ended November 30, 2013, we sold two hyperthermia systems. By comparison, during the three months ended November 30, 2012, we did not sell any hyperthermia systems.

Historically, our revenues have fluctuated significantly from period to period because our sales were based upon a relatively small number of hyperthermia systems, the sales price of each being substantial enough to greatly impact revenue levels in the periods in which they occur. However, we have been unable to sustain an increase in the number of hyperthermia systems sold due to various factors, including: non-acceptance by cancer-treating physicians of hyperthermia therapy; inadequate reimbursement rates from third-party payers; and significant uncertainty in the U.S. healthcare industry due to recent governmental healthcare reform. We believe these difficulties may continue to negatively impact the sales of our hyperthermia systems and our operating results.

At times, we have derived a significant portion of our revenues from sales to related parties. All of our related party revenue results from the sale of hyperthermia systems and related component parts and services to Dr. Sennewald Medizintechnik GmbH. Dr. Sennewald, one of our directors and significant stockholders, is a stockholder, executive officer and a director of Medizintechnik. We derived $16,686, or approximately 1%, of our total revenue in the three months ended November 30, 2013 from sales to related parties, compared to $70,271 or approximately 11%, in the three months ended November 30, 2012. The growth in our revenues has come from non-related parties.

The following tables summarize the sources of our revenues for the three months ended November 30, 2013 and 2012:

	Three Months Ended November 30, 2013	Three Months Ended November 30, 2012
Non-Related Parties		
Product sales	$ 804,400	$ 219,000
Disposable devices	351,710	224,425
Service contracts and other	75,449	74,189
Total	$ 1,231,559	$ 517,614

	Three Months Ended November 30, 2013	Three Months Ended November 30, 2012
Related Parties		
Product sales	$ -	$ 50,000
Disposable devices	10,050	1,350
Service contracts and other	6,636	18,921
Total	$ 16,686	$ 70,271

Gross Margin

Our gross margin and gross margin percentage will fluctuate from period to period depending on the mix of revenues reported for the period and the type and configuration of the hyperthermia systems sold during the period. Our total gross margin was $691,333, or approximately 52% of total revenues, for the three months ended November 30, 2013 and $186,591, or approximately 28%, for the three months ended November 30, 2012. The increase in gross margin and gross margin percentage in the three months ended November 30, 2013 compared to the three months ended November 30, 2012 resulted primarily from 1) increasing MicroThermX sales, particularly sales of consumable devices and equipment rental, and 2) sales of two hyperthermia systems in the three months ended November 30, 2013 compared to no sales of hyperthermia systems in the three months ended November 30, 2012.

Cost of Revenues

Cost of sales includes raw material, labor and allocated overhead costs. We calculate and report separately cost of sales for both non-related and related party sales, which are sales to Medizintechnik. Cost of sales as a percentage of sales will fluctuate from period to period depending on the mix of sales for the period and the type and configuration of the hyperthermia systems sold during the period. Total cost of revenues for the three months ended November 30, 2013 was $639,312 compared to $473,194 for the three months ended November 30, 2012, an increase of $166,118, or approximately 35%. This increase resulted primarily from increasing MicroThermX sales in the first quarter of the current fiscal year compared to the first quarter of last fiscal year, as further discussed above. We also sold two hyperthermia systems in the three months ended November 30, 2013 and no hyperthermia systems in the three months ended November 30, 2012.

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Operating Costs and Expenses

Research and Development Expenses – Research and development expenses include expenditures for new product development and development of enhancements to existing products. Research and development expenses for the three months ended November 30, 2013 were $502,757 which is comparable to $527,267 for the three months ended November 30, 2012, a decrease of $24,510 or 5%.

Selling, General and Administrative Expenses – Selling, general and administrative expenses were $1,704,713 for the three months ended November 30, 2013 compared to $1,889,249 for the three months ended November 30, 2012, a decrease of $184,536, or approximately 10%. Much of this decrease is attributable to the severance accrued to our former Chief Financial Officer in the three months ended November 30, 2012. As we continue to roll out the MicroThermX product line and the support of its global distribution network, we believe that the level of our selling, general and administrative expenses may continue to increase over the levels reported for the first quarter of our current fiscal year, and the increase may be significant.

Other Income (Expense)

During the three months ended November 30, 2013 and 2012, other income (expense) was not material to our operations.

Liquidity and Capital Resources

From inception through November 30, 2013, we have generated an accumulated deficit of $47,141,799 where our operating revenues have been insufficient to cover our operating expenses. We have financed our operations primarily through the sale of our common stock. As of November 30, 2013, we had cash and cash equivalents of $7,580,268, comprised primarily of money market funds and savings accounts. Current assets were $11,562,729, including $1,150,206 of net accounts receivable.

As of November 30, 2013, we had current liabilities totaling $1,969,991, comprised of accounts payable, accrued liabilities, customer deposits and deferred revenue incurred in the normal course of our business. Our long-term liabilities consisted of deferred revenue of $47,014.

Shelf Registration Statement and April 2013 Stock Offering

On September 28, 2012, we filed a universal shelf registration statement (Form S-3; file number 333-184164) with the SEC for the issuance of common stock, preferred stock, warrants, senior debt, subordinated debt and units up to an aggregate amount of $50.0 million. On October 11, 2012, the universal shelf registration statement was declared effective by the SEC. We may periodically offer one or more of these securities in amounts, prices and terms to be announced when and if the securities are offered. At the time any of the securities covered by the registration statement are offered for sale, a prospectus supplement will be prepared and filed with the SEC containing specific information about the terms of any such offering.

In April 2013, we completed an offering of 4,065,042 shares of our common stock and warrants to purchase a total of 3,048,782 shares of our common stock with certain institutional investors (the “Offering”). The Offering was completed using our shelf registration statement, and net proceeds to us were approximately $4.6 million.

The warrants became exercisable six months and one day following the closing date of the Offering and will remain exercisable for five years thereafter at an exercise price of $1.65 per share. The exercise price of the warrants is subject to adjustment in the case of stock splits, stock dividends, combinations of shares and similar recapitalization transactions. The exercisability of the warrants may be limited if, upon exercise, the holder or any of its affiliates would beneficially own more than 4.9% of our common stock.

We agreed with each of the purchasers that, subject to certain exceptions, we will not, within the 30 trading days following the closing of the Offering (which period may be extended in certain circumstances), enter into any agreement to issue or announce the issuance or proposed issuance of any securities.

We also agreed with each of the purchasers that while the warrants are outstanding, we will not affect or enter into an agreement to affect a "Variable Rate Transaction," which means a transaction in which we:

- Issue or sell any convertible securities either (A) at a conversion, exercise or exchange rate or other price that is based upon and/or varies with the trading prices of, or quotations for, the shares of our common stock at any time after the initial issuance of such convertible securities, or (B) with a conversion, exercise or exchange price that is subject to being reset at some future date after the initial issuance of such convertible securities or upon the occurrence of specified or contingent events directly or indirectly related to our business or the market for our common stock, other than pursuant to a customary "weighted average" anti-dilution provision; or

- Enter into any agreement (including, without limitation, an equity line of credit) whereby we may sell securities at a future determined price (other than standard and customary "preemptive" or "participation" rights).

We also agreed with each of the purchasers if we issue securities within the 12 months following the closing of the Offering, the purchasers shall have the right to purchase all of the securities on the same terms, conditions and price provided for in the proposed issuance of securities.

We also agreed to indemnify each of the purchasers against certain losses resulting from our breach of any of our representations, warranties, or covenants under agreements with each of the purchasers, as well as under certain other circumstances described in the Purchase Agreement.

Cash Flows from Operating, Investing and Financing Activities

During the three months ended November 30, 2013, we used net cash of $1,858,484 in operating activities, primarily as a result of our net loss of $1,512,861, decreased by non-cash expenses totaling $246,350, including depreciation and amortization and stock-based compensation. Net cash used in operating activities also included increases in receivables of $266,923 and inventories of $184,644, and decreases in accounts payable of $9,544, accrued liabilities of $157,840 and deferred revenue of $29,193, partially offset by a decrease in other current assets of $39,074 and an increase in customer deposits of $17,097.

During the three months ended November 30, 2012, we used net cash of $1,955,831 in operating activities, primarily as a result of our net loss of $2,218,664, decreased by non-cash expenses totaling $327,184, including depreciation and amortization and stock-based compensation. Net cash used in operating activities also included increases in receivables of $170,244 and other current assets of $16,304, and a decrease in deferred revenue of $3,318, partially offset by a decrease in inventories of $59,899 and increases in accounts payable of $14,590, accrued liabilities of $34,756 and customer deposits of $16,270.

Net cash used in investing activities, resulting from the purchase of property and equipment, was $11,776 and $4,160 for the three months ended November 30, 2013 and 2012, respectively.

We had no net cash provided by or used in financing activities for the three months ended November 30, 2013 and 2012.

We believe that our current cash and cash equivalents will be sufficient to fund our operations for the next twelve months.

If we cannot cover any future cash shortfalls with cost cutting or available cash, or our sales are less than projected, we would need to obtain additional financing. We cannot be certain or provide any assurance that any financing will be available when needed or will be available on terms acceptable to us. If we raise equity capital, our stockholders will be diluted. Insufficient funds may require us to delay, scale back or eliminate some or all of our programs designed to facilitate the commercialization of our systems or entry into new markets.

As of November 30, 2013, we had no significant commitments for the purchase of property and equipment.

We had no material off balance sheet arrangements as of November 30, 2013.

Critical Accounting Policies

The following is a discussion of our critical accounting policies and estimates that management believes are material to an understanding of our results of operations and which involve the exercise of judgment or estimates by management.

Revenue Recognition: Revenue from the sale of cancer treatment systems is recognized when a purchase order has been received, the system has been shipped, the selling price is fixed or determinable, and collection is reasonably assured. Most system sales are F.O.B. shipping point; therefore, shipment is deemed to have occurred when the product is delivered to the transportation carrier. Most system sales do not include installation. If installation is included as part of the contract, revenue is not recognized until installation has occurred, or until any remaining installation obligation is deemed to be perfunctory. Some sales of systems may include training as part of the sale. In such cases, the portion of the revenue related to the training, calculated based on the amount charged for training on a stand-alone basis, is deferred and recognized when the training has been provided. The sales of our cancer treatment systems do not require specific customer acceptance provisions and do not include the right of return except in cases where the product does not function as warranted by us, or are not within product specifications. To date, returns have not been significant.

Revenue from the sale of disposable devices is recognized when a purchase order has been received, the devices have been shipped, the selling price is fixed or determinable, and collection is reasonably assured. Currently, our customers are not required to purchase a minimum number of disposable devices in connection with the purchase of our systems.

Revenue from training services is recorded when an agreement with the customer exists for such training, the training services have been provided, and collection is reasonably assured.

Revenue from service support contracts is recognized on a straight-line basis over the term of the contract, which approximates recognizing it as it is earned.

Revenue from equipment rental under an operating lease is recognized when billed in accordance with the lease agreement.

Our revenue recognition policy is the same for sales to both related parties and non-related parties. We provide the same products and services under the same terms for non-related parties as with related parties.

Sales to distributors are recognized in the same manner as sales to end-user customers.

Deferred revenue and customer deposits include amounts from service contracts as well as cash received for the sales of products, which have not been shipped.

Inventory Reserves: We maintain a reserve for obsolete inventories to reduce excess and obsolete inventories to their estimated net realizable value. This reserve is a significant estimate and we periodically review our inventory levels and usage, paying particular attention to slower-moving items. If projected sales do not materialize or if our systems do not receive increased market acceptance, we may be required to increase the reserve for obsolete inventories in future periods.

Product Warranty: We provide limited product warranties on our systems. These warranties vary from contract to contract, but generally consist of parts and labor warranties for one year from the date of installation. To date, expenses resulting from such warranties have not been material. We record a warranty expense at the time of each sale. This reserve is estimated based on prior history of service expense associated with similar units sold in the past.

Allowance for Doubtful Accounts: We maintain an allowance for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. This allowance is a significant estimate and is regularly evaluated by us for adequacy by taking into consideration factors such as past experience, credit quality of the customer base, age of the receivable balances, both individually and in the aggregate, and current economic conditions that may affect a customer’s ability to pay. If the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required.

Stock-based Compensation: Stock-based compensation cost of stock options and other stock-based awards to employees and directors is measured at the grant date based on the estimated value of the award granted, using the Black-Scholes option pricing model, and recognized over the period in which the award vests. For stock awards no longer expected to vest, any previously recognized stock compensation expense is reversed in the period of termination. The stock-based compensation expense has been allocated to the various categories of operating costs and expenses in a manner similar to the allocation of payroll expense. The Black-Scholes valuation model utilizes inputs that are subject to change over time, including the volatility of the market price of our common stock, risk free interest rates, requisite service periods and assumptions made by us regarding the assumed life and vesting of stock options and stock-based awards. As new options or stock-based awards are granted, additional non-cash compensation expense will be recorded by us.

Income Taxes: We account for income taxes using the asset and liability method. Under the asset and liability method, deferred tax assets and liabilities are recognized for the future consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. 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 of a change in tax rates is recognized in income in the period that includes the enactment date.

We maintain valuation allowances where it is more likely than not that all or a portion of a deferred tax asset will not be realized. Changes in valuation allowances are included in our income tax provision in the period of change. In determining whether a valuation allowance is warranted, we evaluate factors such as prior earnings history, expected future earnings and our ability to carry back reversing items within two years to offset income taxes previously paid.

To the extent that we have the ability to carry back current period taxable losses to offset income taxes previously paid, we record an income tax receivable and a current income tax benefit.

Recent Accounting Pronouncements

No new accounting pronouncements were adopted during the quarter ended November 30, 2013 that had a material impact on our financial statements. No new accounting pronouncements were issued during the three months ended November 30, 2013 and through the date of filing this report that we believe are applicable or would have a material impact on our financial statements.

Medical Device Excise Tax:

A Medical Device Excise Tax (MDET) was enacted into law as part of the Health Care Education Reconciliation Act of 2010 and imposes an excise tax on medical device manufacturers on their sales in the U.S of certain devices after December 31, 2012. The tax is 2.3% of the taxable base.

FORWARD-LOOKING STATEMENTS

With the exception of historical facts, the statements contained in "Management's Discussion and Analysis of Financial Condition and Results of Operations" and other parts of this quarterly report on Form 10-Q are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, which reflect our current expectations and beliefs regarding our future results of operations, performance and achievements. These statements are subject to risks and uncertainties and are based upon assumptions and beliefs that may or may not materialize. These forward-looking statements include, but are not limited to, statements concerning:

- our belief about the market opportunities for our products;
- our anticipated financial performance and business plan;
- our belief that the distribution agreement with Terumo Europe NV will drive market adoption of the MicroThermX®;
- our expectations that we will continue and grow the successful results from our MicroThermX fee-per-use equipment rental program throughout the U.S. that we have experienced to date;
- our expectations that the SynchroWave antennas used in conjunction with the MicroThermX will represent a significant ongoing revenue stream;
- our expectations that we will reach agreements with additional international distribution firms;
- our expectations that additional international shipments of the MicroThermX and supplies of SynchroWave antennas will occur in calendar year 2014;
-

our belief that the level of our operating expenses, including selling, general and administrative expenses, will increase and that the increase may be significant;

- our belief that our operating results, revenue and operating expenses may fluctuate in the future from year to year as well as from quarter to quarter; and

- our belief that our current cash and cash equivalents will be sufficient to finance our operations for the next twelve months.

We wish to caution readers that the forward-looking statements and our operating results are subject to various risks and uncertainties that could cause our actual results and outcomes to differ materially from those discussed or anticipated, including the factors set forth in Item 1A – "Risk Factors" in our Annual Report on Form 10-K for the year ended August 31, 2013 and our other filings with the Securities and Exchange Commission. We also wish to advise readers not to place any undue reliance on the forward-looking statements contained in this report, which reflect our beliefs and expectations only as of the date of this report. We assume no obligation to update or revise these forward-looking statements to reflect new events or circumstances or any changes in our beliefs or expectations, other than as required by law.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

There are no material changes to our market risk as described in our annual report on Form 10-K for the year ended August 31, 2013

Item 4. Controls and Procedures

Evaluation of disclosure controls and procedures.

As of the end of the period covered by this report, we conducted an evaluation, under the supervision and with the participation of our management including our principal executive officer and principal financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) or 15d-15(e) under the Securities Exchange Act of 1934 ("Exchange Act"). Based on this evaluation, the principal executive officer and principal accounting officer concluded that, as of the end of the period covered by this report, our disclosure controls and procedures were effective in ensuring that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in applicable rules and forms and that such information is accumulated and communicated to our management, including our principal executive officer and principal financial officer, in a manner that allows timely decisions regarding required disclosure.

Changes in internal controls over financial reporting.

There was no change in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) during our most recently completed fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

Item 1A. Risk Factors

In addition to the other information set forth in this report, you should carefully consider the risk factors reported in our Annual Report on Form 10-K for the year ended August 31, 2013.

Item 6. Exhibits

The following exhibits are filed as part of this report:

Exhibit No.	Description of Exhibit
31.1	Certification of the Principal Executive Officer Required Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of the Principal Financial Officer Required Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Principal Executive Officer Required Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Principal Financial Officer Required Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Extension Schema
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase
101.DEF*	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB*	XBRL Taxonomy Extension Label Linkbase
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase

* The XBRL related information in Exhibit 101 shall not be deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to liability of that section and shall not be incorporated by reference into any filing or other document pursuant to the Securities Act of 1933, as amended, except as shall be expressly set forth by specific reference in such filing or document.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

BSD MEDICAL CORPORATION

Date: January 9, 2014	/s/ Harold R. Wolcott Harold R. Wolcott President (Principal Executive Officer and Duly Authorized Officer)
Date: January 9, 2014	/s/ William S. Barth William S. Barth Chief Financial Officer (Principal Financial Officer and Duly Authorized Officer)