

Edgar Filing: CAPRIUS INC - Form 10QSB

CAPRIUS INC
Form 10QSB
February 22, 2005

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

FORM 10-QSB

(Mark one)

Quarterly Report under Section 13 or 15 (d) of the
Securities Exchange Act of 1934

FOR THE QUARTERLY PERIOD ENDED DECEMBER 31, 2004

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

Commission File Number: 0-11914

CAPRIUS, INC.

(Exact name of small business issuer as specified in its charter)

Delaware

22-2457487

(State or other jurisdiction of
incorporation or organization)

(I.R.S. Employer
Identification No.)

One Parker Plaza, Fort Lee, NJ 07024

(Address of principal executive offices) (Zip Code)

Issuer's telephone number: (201) 592-8838

N/A

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

Indicate by check mark whether the registrant (1) filed all reports
required to be filed under Section 13 or 15 (d) of the Exchange Act during the
past 12 months (or for such shorter period that the Registrant was required to
file such reports), and (2) has been subject to such filing requirements for the
past 90 days. Yes No

State the number of shares outstanding of issuer's classes of common
equity, as of the latest practicable date.

Class
Common Stock. Par value \$0.01

Outstanding at February 18, 2005
20,446,562 shares

Edgar Filing: CAPRIUS INC - Form 10QSB

CAPRIUS, INC. AND SUBSIDIARIES

INDEX

	Page No. -----
PART I - FINANCIAL INFORMATION	
ITEM 1. UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS	
Condensed Consolidated Balance Sheet as of December 31, 2004	3
Condensed Consolidated Statements of Operations for the three months ended December 31, 2004 and 2003	4
Condensed Consolidated Statements of Cash Flows for the three months ended December 31, 2004 and 2003	5
Notes to Condensed Consolidated Financial Statements	6
ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS	11
ITEM 3. CONTROLS & PROCEDURES	14
PART II - OTHER INFORMATION	
ITEM 1. LEGAL PROCEEDINGS	14
ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K	15
SIGNATURES	17

CAPRIUS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEET
(UNAUDITED)

December 31, 2004

ASSETS

CURRENT ASSETS:

Cash and cash equivalents	\$ 19,146
Accounts receivable, net of reserve for bad debts of \$5,163	57,828
Inventories, net	754,685
Due from sale of Strax	33,000
Deferred financing costs, net of accumulated amortization of \$102,333	51,167
Other current assets	6,223

Edgar Filing: CAPRIUS INC - Form 10QSB

Total current assets	922,049

PROPERTY AND EQUIPMENT:	
Office furniture and equipment	167,221
Equipment for lease	76,666
Leasehold improvements	19,536

	263,423
Less: accumulated depreciation	203,839

Property and equipment, net	59,584

OTHER ASSETS:	
Goodwill	737,010
Intangible assets, net of accumulated amortization of \$565,083	474,917
Other	13,330

Total other assets	1,225,257

TOTAL ASSETS	\$ 2,206,890
	=====
LIABILITIES AND STOCKHOLDERS' DEFICIENCY	
CURRENT LIABILITIES:	
Secured convertible notes, net of unamortized discount of \$100,000	\$ 1,400,000
Notes payable - related party, net of unamortized discount of \$10,653	628,140
Accounts payable	1,146,729
Accrued expenses	438,202
Accrued compensation	290,077

Total current liabilities	3,903,148

STOCKHOLDERS' DEFICIENCY:	
Preferred stock, \$.01 par value	
Authorized - 1,000,000 shares	
Issued and outstanding - Series A, none; Series B, convertible, 27,000 shares . Liquidation preference \$2,700,000	2,700,000
Common stock, \$.01 par value	
Authorized - 50,000,000 shares, issued 20,469,062 shares and outstanding 20,446,562 shares	204,691
Additional paid-in capital	67,837,158
Accumulated deficit	(72,435,857)
Treasury stock (22,500 common shares, at cost)	(2,250)

Total stockholders' deficiency	(1,696,258)

TOTAL LIABILITIES AND STOCKHOLDERS' DEFICIENCY	\$ 2,206,890
	=====

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

Edgar Filing: CAPRIUS INC - Form 10QSB

CAPRIUS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

	For the Three Months Ended	
	December 31, 2004	December 31, 2003
REVENUES:		
Product sales	\$ 236,908	\$ 258,800
Equipment rental income	5,326	18,300
Consulting and royalty fees	20,425	12,500
	262,659	289,600
OPERATING EXPENSES:		
Cost of product sales and equipment rental income	161,794	204,700
Research and development	76,580	39,500
Selling, general and administrative	672,278	674,200
	910,652	918,400
Operating loss	(647,993)	(628,800)
Interest expense, net	(149,079)	(40,000)
Loss from continuing operations	(797,072)	(629,200)
Loss from operations of discontinued Strax business	-	(28,400)
Net loss	\$ (797,072)	\$ (657,600)
Net loss per basic and diluted common share:		
Continuing operations	\$ (0.04)	\$ (0.04)
Discontinued operations	-	-
Net loss per basic and diluted common share	\$ (0.04)	\$ (0.04)
Weighted average number of common shares outstanding, basic and diluted	20,446,562	20,446,562

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

Edgar Filing: CAPRIUS INC - Form 10QSB

CAPRIUS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

	Three Months Ended December 31, 2004	2003
	-----	-----
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	\$ (797,072)	\$ (657,676)
Adjustments to reconcile net loss to net cash used in operating activities:		
Amortization of debt discount	54,567	-
Amoritization of deferred financing costs	38,375	-
Depreciation and amortization	81,422	62,328
Changes in operating assets and liabilities:		
Accounts receivable	15,654	39,280
Inventories	22,011	2,432
Other assets	8,999	(105,408)
Accounts payable and accrued expenses	397,250	(205,461)
	-----	-----
Net cash used in operating activities	(178,794)	(864,505)
	-----	-----
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sale of Strax business	33,000	213,190
Acquistion of property and equipment	(1,436)	(1,886)
	-----	-----
Net cash provided by investing activities	31,564	211,304
	-----	-----
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from issuance of notes payable - related party	138,793	-
	-----	-----
Net cash provided by financing activities	138,793	-
	-----	-----
NET DECREASE IN CASH AND CASH EQUIVALENTS	(8,437)	(653,201)
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	27,583	774,819
	-----	-----
CASH AND CASH EQUIVALENTS, END OF PERIOD	\$ 19,146	\$ 121,618
	=====	=====
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid for interest during the period	\$ -	\$ 115
	=====	=====
NON CASH-FLOW ITEM:		
Transfer of net book value of certain equipment for leases		

Edgar Filing: CAPRIUS INC - Form 10QSB

to inventory	\$ 66,177	\$ -
	=====	=====

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

5

CAPRIUS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

NOTE 1 - BASIS OF PRESENTATION

The condensed consolidated balance sheet as of December 31, 2004, and the condensed consolidated statements of operations and cash flows for the three month periods ended December 31, 2004 and 2003, have been prepared by the Company without audit. In the opinion of management, the information contained herein reflects all adjustments necessary to make the presentation of the Company's condensed financial position, results of operations and cash flows not misleading. All such adjustments are of a normal recurring nature.

The accompanying condensed consolidated financial statements do not contain all of the information and disclosures required by accounting principles generally accepted in the United States of America and should be read in conjunction with the consolidated financial statements and related notes included in the Company's annual report on Form 10-KSB for the fiscal year ended September 30, 2004.

NOTE 2 - THE COMPANY

Caprius, Inc. ("Caprius", the "Company", "we", "us" and "our") is engaged in the infectious medical waste disposal business. In the first quarter of Fiscal 2003, we acquired a majority interest in M.C.M. Environmental Technologies, Inc. ("MCM") which developed, markets and sells the SteriMed and SteriMed Junior compact systems that simultaneously shred and disinfect Regulated Medical Waste. The SteriMed Systems are sold and leased in both the domestic and international markets.

In December 2002, the Company closed the acquisition of our initial investment of 57.53% of the capital stock of MCM for a purchase price of \$2.4 million. MCM wholly-owns MCM Environmental Technologies Ltd., an Israeli corporation, which initially developed the SteriMed Systems. Upon closing, our designees were elected to three of the five seats on MCM's Board of Directors, with George Aaron, President and CEO, and Jonathan Joels, CFO, filling two seats. Additionally, as part of the transaction, certain debt of MCM to its existing stockholders and to certain third parties was converted to equity in MCM or restructured. Pursuant to its Letter of Intent with MCM, Caprius had provided MCM with loans totaling \$565,000, which loans were repaid upon closing by a reduction in the cash portion of the purchase price. As part of the Stockholders Agreement dated December 17, 2002, there were certain provisions relating to performance adjustments for the twenty four month period post closing. As a consequence, the Company's ownership interest increased by 5% in the fiscal year 2004. For the six month period that commenced on July 17, 2004 and ends on January 17, 2005, pursuant to a Stockholders Agreement, the stockholders of MCM (other than the Company) have the right to put all of their

Edgar Filing: CAPRIUS INC - Form 10QSB

MCM shares to MCM, and MCM has the right to call all of such shares not currently owned by us. In accordance with the Stockholders Agreement dated December 17, 2002, the party who first exercises its put or call rights is required to accompany its notice of put or call with its proposal for the price of the stock interest in MCM to be sold or purchased, as applicable. The recipient is then required to give notice to the exercising party of its proposed price for such interest. The parties shall then negotiate and agree upon an agreed price. At our option, we may pay the purchase price for the remaining MCM shares in cash or in shares of our common stock. Neither party gave notice of its put or call.

During the first quarter of fiscal year 2005, an agreement was reached between the Company and the 20% minority ownership of an MCM subsidiary which has been dormant since inception. The minority shareholders shall be repaid their initial investment, by way of a credit towards the site installation expense of SteriMed units that they are purchasing for their dialysis centers. This subsidiary was dissolved on February 9, 2005.

6

NOTE 3 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Stock Based Compensation

At December 31, 2004, the Company had three stock based compensation plans (one incentive and nonqualified, one employee and one non-employee director plan). The Company accounts for these plans under the recognition and measurement principles of APB Opinion No. 25, "Accounting for Stock Issued to Employees," and complies with the disclosure requirements of Statement of Financial Accounting Standards ("SFAS") No. 123, "Accounting for Stock-based Compensation" as amended by SFAS No. 148, "Accounting for Stock-based Compensation - Transition and Disclosure, an amendment of SFAS No. 123, issued in December 2002. Under APB Opinion No. 25, compensation expense is based on the difference, if any, generally on the date of grant, between the fair value of our stock and the exercise price of the option. No stock-based employee compensation cost is reflected within the statement of operations for the three month periods ended December 31, 2004 and 2003.

If the Company had elected to recognize compensation costs for the Company's option plans using the fair value method at the grant dates, the effect on the Company's net loss and loss per share for the periods shown below would have been as follows:

	Three months ended December 31,	
	2004	2003
	-----	-----
Net loss as reported	\$ (797,072)	\$ (657,676)
Deduct:		
Stock-based employee compensation determined under fair value method for all awards, net of related tax effects	(818)	(13,687)

Edgar Filing: CAPRIUS INC - Form 10QSB

	-----	-----
Pro forma net loss	\$ (797,890)	\$ (671,363)
	=====	=====
Basic and diluted loss per share of Common Stock		
As reported	\$ (0.04)	\$ (0.03)
Pro forma	\$ (0.04)	\$ (0.03)

Loss Per Share

The Company follows Statement of Financial Accounting Standards (SFAS) No. 128, "Earnings Per Share", which provides for the calculation of "basic" and "diluted" earnings (loss) per share. Basic loss per share includes no dilution and is computed by dividing loss available to common stockholders by the weighted-average number of common shares outstanding for the period. Diluted loss per share reflects the potential dilution that could occur through the effect of common shares issuable upon the exercise of stock options and warrants and convertible securities. For the periods ended December 31, 2004 and 2003, potential common shares amount to 16,898,215 and 6,854,867 respectively, and have not been included in the computation of diluted loss per share since the effect would be antidilutive.

7

Revenue Recognition

The medical infectious waste business recognizes revenues from either the sale or rental of its SteriMed units. Revenues for sales are recognized at the time that the unit is shipped to the customer. Rental revenues are recognized based upon either services provided for each month of activity or evenly over the year in the event that a fixed rental agreement is in place.

Impairment of Long-Lived Assets

In accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," the Company and its subsidiaries review the carrying values of their long-lived assets (other than goodwill) for possible impairment whenever events or changes in circumstances indicate that the carrying amounts of the assets may not be recoverable. Any long-lived assets held for disposal are reported at the lower of their carrying amounts or fair values less costs to sell.

Goodwill and Other Intangibles

The Company has adopted the provisions of SFAS No. 141, "Business Combinations," and SFAS No. 142, "Goodwill and Other Intangible Assets". SFAS No. 141 is effective as to any business combination occurring after June 30, 2001 and certain transition provisions that affect accounting for business combinations prior to June 30, 2001 are effective as of the date SFAS No. 142 is applied in its entirety. Goodwill relating to acquisitions completed subsequent to June 30, 2001 is not amortized and is subject to impairment testing. In addition, effective January 1, 2002, the Company will no longer be required to amortize goodwill and certain other intangibles assets relating to acquisitions

Edgar Filing: CAPRIUS INC - Form 10QSB

completed prior to July 1, 2001.

SFAS No. 142 provides, among other things, that goodwill and intangible assets with indeterminate lives shall not be amortized. Goodwill shall be assigned to a reporting unit and annually tested for impairment. Intangible assets with determinate lives shall be amortized over their estimated useful lives, with the useful lives reassessed continuously, and shall be assessed for impairment under the provisions of SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of". Goodwill is also assessed for impairment on an interim basis when events and circumstances warrant. The Company assesses whether an impairment loss should be recognized and measured by comparing the fair value of the "reporting unit" to the carrying value, including goodwill. If the carrying value exceeds fair value, then the Company will compare the implied fair value of the goodwill (as defined in SFAS No. 142) to the carrying amount of the goodwill. If the carrying amount of the goodwill exceeds the implied fair value, then the goodwill will be adjusted to the implied fair value. At September 30, 2004, goodwill results from the excess of cost over the fair value of net assets acquired related to the MCM business.

NOTE 4 - INVENTORIES

Inventories consist of the following, net of reserves of approximately \$34,200 for the period ended December 31, 2004:

	December 31, 2004 ----
Raw materials	\$315,523
Finished goods	439,162 -----
	\$754,685 =====

NOTE 5 - NOTES PAYABLE

During the third quarter of fiscal 2004, the Company raised an aggregate of \$1.5 million through the issuance of 8% Senior Secured Convertible Promissory Notes ("the Notes"), prior to underwriting fees and expenses. The proceeds were used for general working capital. The Company granted a security interest in

substantially all of the assets of the Company. The Notes mature in one year and can be converted into shares of common stock at the election of the investor at any time using a conversion price of \$0.20 per share. Certain conditions were not met as of September 30, 2004, and therefore the conversion price was reduced to \$0.15 per share. The beneficial conversion feature of the Notes, amounted to \$200,000 and as such the amount was treated as a discount to debt and a corresponding increase to paid in capital. This amount is being amortized over the life of the loan. Amortization for the three month period ended December 31, 2004 amounted to \$50,000 and that amount is included in interest expense, net in the consolidated statement of operations. The financing was arranged through

Edgar Filing: CAPRIUS INC - Form 10QSB

Sands Brothers International Ltd. ("Sands") who were retained by the Company to act as selected dealer for the sale and issuance of the Notes. Based upon the funds raised, Sands received a six percent fee and an expense allowance of one percent of the gross proceeds and warrants valued at \$28,500 using the Black Scholes Model to purchase 1,425,000 shares of the Company's common stock at an exercise price of \$0.28 per share for a period of five years. The total fees for the offering were \$125,000. The debt issuance costs are being amortized over the term of the loan. Amortization for the three month period ended December 31, 2004 amounted to \$38,375 and that amount is included in interest expense, net in the consolidated statement of operations. On February 15, the Company closed on a \$4.5 million preferred stock equity financing (see Note 9). As a condition of this financing, the holders of the Notes amended and converted their Notes together with accrued interest, into an aggregate of 15,953 shares of Series C Mandatory Convertible Preferred Stock.

NOTE 6 - NOTES PAYABLE - RELATED PARTY TRANSACTIONS

During the three month period ended December 31, 2004, the Company was advanced the principal amount of approximately \$138,790 through short term loans until additional equity funding was secured. The terms of the loans are identical to the terms of the \$100,000 8% Senior Secured Convertible Promissory Note outlined in Note 9. The allocated fair value of the warrants associated with this advance are deemed to be immaterial. These short-term loans were provided by executive officers, Messrs. Aaron, Joels, and Koppel who advanced approximately \$64,000, 62,350 and \$12,440, respectively. These funds were utilized for general working capital purposes. As a condition of this financing, the holders of the Notes exchanged 50% of their indebtedness for 694 shares of Series C Mandatory Convertible Preferred Stock and were paid the balance of their notes inclusive of interest from the net proceeds of the \$4.5 million preferred stock equity financing of February 15, 2005 (see Note 9) and the security interest was terminated.

During the second quarter of fiscal 2004, the Company authorized a short-term bridge loan for an aggregate of \$500,000 through the issuance of loan notes due on July 31, 2005. The funds were utilized primarily for general working capital. The majority of the funds were provided by management of the Company. The loan notes bear interest at a rate of 11% per annum and were secured by a first lien on any royalties received by Opus Diagnostics Inc. from Seradyn, Inc. in accordance with their Royalty Agreement. For every three dollars (\$3.00) loaned, the lender received two warrants to purchase one share of Common Stock, exercisable at \$0.25 per share for a period of five years. The warrants were valued at \$27,400 using the Black Scholes Model and such amount was treated as a discount to debt and a corresponding increase to paid in capital. The discount is being amortized over the life of the loan. For the three month period ended December 31, 2004, the Company recorded an additional interest expense related to this discount of approximately \$4,600, and that amount is included in interest expense, net in the consolidated statement of operations. On February 15, 2005 the Company closed on a \$4.5 million preferred stock equity financing (see Note 9). As a condition of this financing the holders of the Notes converted their notes, into an aggregate of 5,000 shares of Series C Mandatory Convertible Preferred Stock and the security interest was terminated.

NOTE 7 - ECONOMIC DEPENDENCY

For the three months ended December 31, 2004, revenue from four customers was approximately \$91,000, \$56,000, \$42,000 and \$41,000 which represented approximately 88% of the total revenue. At December 31, 2004 accounts receivable from these customers were approximately \$0, \$45,267, \$0, and \$0 respectively.

Edgar Filing: CAPRIUS INC - Form 10QSB

9

For the three months ended December 31, 2003, revenue from two customers was approximately \$121,000 (2004 - \$56,000) and \$124,000 (2004 - \$41,000), which represented approximately 85% of the total revenue.

NOTE 8 - LITIGATION

In June 2002, Jack Nelson, a former Caprius executive officer and director, commenced two legal proceedings against us and George Aaron and Jonathan Joels, executive officers, directors and principal stockholders. The two complaints alleged that the individual defendants made misrepresentations to the plaintiff upon their acquisition of a controlling interest in the Company in 1999 and thereafter made other alleged misrepresentations and engaged in mismanagement and other misconduct and took other actions as to the plaintiff to the supposed detriment of the plaintiff and Caprius. One action was brought in Superior Court of New Jersey, Bergen County ("State Court Action"), and the other was brought as a derivative action in Federal District Court in New Jersey ("Federal Derivative Action"). In September 2003, we resolved the State Court Action by making an Offer of Judgment which was accepted by the plaintiff. Under the terms of the Offer of Judgment, which was made without any admission or finding of liability on part of the defendants, we paid \$125,000 to the plaintiff and the action was discontinued.

On May 3, 2004, the Court in the Federal Derivative Action granted the motion made by us and Messrs. Aaron and Joels for judgment on the pleadings based upon the pre-suit demand requirement and dismissed the plaintiff's complaint without prejudice, but denied defendants' motion for judgment on the pleadings based upon the Private Securities Litigation Reform Act. The Court also granted the plaintiff's cross-motion to file an amended complaint to add allegations of insider trading.

In September 2002, we were served with a complaint naming us and our principal officers and directors in the Federal District Court of New Jersey as a purported class action (the "Class Action"). The allegations in the complaint cover the period between February 14, 2000 and June 20, 2002. The initial plaintiff is a relative of the wife of the plaintiff in the State Court Action and Federal Derivative Action. The allegations in the purported Class Action were substantially similar to those in the other two Actions. The complaint sought an unspecified amount of monetary damages, as well as the removal of the defendant officers as shareholders.

On May 3, 2004, in a decision separate from the decision in the Federal Derivative Action, the Court granted the defendants' motion and dismissed the Class Action. The federal securities claims asserted by the plaintiffs were dismissed with prejudice, and having dismissed all federal law claims, the Court declined to exercise jurisdiction over the remaining state law claims and dismissed those claims without prejudice. On May 14, 2004, the plaintiffs filed a motion for reconsideration, which defendants opposed and subsequently this motion for reargument was denied. The plaintiff did not file a notice of appeal during the statutory time period.

On September 30, 2004, our Board received a letter written from Mr. Nelson's attorney making a demand that we institute a derivative action substantially similar to the allegations presented in the Federal Derivative Action. A draft complaint was included with the letter. An Independent Committee of the Board responded to the letter within the stipulated 90 day period that Mr. Nelson had requested, stating that the Independent Committee determined that

Edgar Filing: CAPRIUS INC - Form 10QSB

there was no basis for the Company to institute the derivative action as demanded. There has been no further communication from Mr. Nelson's attorney.

The independent directors have authorized us to advance the legal expenses of Messrs. Aaron and Joels in these litigations with respect to claims against them in their corporate capacities, subject to review of the legal bills and compliance with applicable law, and Messrs. Aaron and Joels will repay us in the event it was determined that they were not entitled to be indemnified as to the claim for which the advance was made.

NOTE 9 - SUBSEQUENT EVENTS

On February 2, 2005, the Company raised \$100,000 through the issuance of 8% Senior Secured Convertible Promissory Notes, repayable, together with interest to April 3, 2005, subject to prepayment in the event of an equity financing in excess of \$2 Million, or conversion by the investors into shares of our common

10

stock at a conversion price of \$0.15 per share. The lenders also received warrants to purchase 100,000 shares of our common stock exercisable at \$0.28 per share for a period of five years. The allocated fair value of these warrants are deemed to be immaterial. In the event that the loan is not repaid as of the due date, then the lender shall receive a further 25,000 warrants per month, up to an aggregate, including the initial 100,000 warrants, of 300,000 warrants. The funds were utilized for general working capital. On February 17, 2005, the Company repaid this loan together with interest.

On February 13, 2005, the Board of Directors approved the issuance of a series of preferred stock to be designated as Series C Mandatory Convertible Preferred Stock, \$0.01 par value, stated value \$100 per share, consisting of 75,000 shares with terms as set forth in the Certificate of Designations, Preferences and Rights.

On February 15, 2005, the Company closed on a \$4.5 million preferred stock equity financing before financing related fees and expenses of approximately \$450,000. The Company issued 45,000 shares of Series C Mandatory Convertible Preferred Stock at a stated value of \$100 per share. The Company also issued Series A Warrants to purchase an aggregate of 9,310,344 shares of common stock at an exercise price of \$0.28 per share for a period of five years. In addition, the Company issued Series B Warrants to purchase an aggregate of 3,103,448 shares of common stock at an exercise price of \$0.145 per share for a period of five years exercisable after nine months, subject to a termination condition defined under Warrant B, Section 18. Simultaneously, the Company converted the short-term secured debt outstanding in the aggregate of \$2 million, together with \$72,962 of unsecured indebtedness, into 21,681 shares of Series C Mandatory Convertible Preferred Stock. As part of the condition for raising the equity financing, holders of a majority of the outstanding shares irrevocably undertook to effect a 1:20 reverse stock split of any outstanding shares of common stock. At the time that the reverse split becomes effective, all of the preferred stock issued to the new equity investors and the debt holders who converted their debt will automatically convert into common shares at a conversion price of \$0.145 per share and/or 2,299,345 shares of the Company's common stock (post reverse split), subject to adjustment in certain circumstances. The Company also agreed to increase the number of independent directors by one additional director.

During the period from January 1, 2005 through February 15, 2005, the Company was advanced the principal amount of approximately \$7,100 through short

Edgar Filing: CAPRIUS INC - Form 10QSB

term loans until additional equity funding is secured. The terms of the loans are identical to the terms of the \$100,000 8% Senior Secured Convertible Promissory Note outlined above. The allocated fair value of the warrants associated with this advance are deemed to be immaterial. These short-term loan was provided by an executive officer, Mr. Koppel. The funds were utilized for general working capital purposes. As a condition of this financing, Mr. Koppel exchanged 50% of his indebtedness for Series C Mandatory Convertible Preferred Stock and on February 15, 2005 was paid the balance inclusive of interest.

ITEM 2: MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITIONS AND RESULTS OF OPERATIONS

FORWARD LOOKING STATEMENTS

The Company is including the following cautionary statement in this Quarterly Report of Form 10-QSB to make applicable and take advantage of the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 for any forward-looking statements made by, or on behalf of, the Company. Forward-looking statements include statements concerning plans, objectives, goals, strategies, future events or performance and underlying assumptions and other statements which are other than statements of historical facts. Certain statements contained herein are forward-looking statements and accordingly involve risks and uncertainties which could cause actual results or outcomes to differ materially from those expressed in the forward-looking statements. The Company's expectations, beliefs and projections are expressed in good faith and are believed by the Company to have a reasonable basis, including without limitation, management's examination of historical operating trends, data contained in the Company's records and other data available from third parties, but there can be no assurance that management's expectation, beliefs or projections will result or be achieved or accomplished. In addition to other factors and matters discussed elsewhere herein, the following are important factors that, in the view of the Company, could cause actual results to differ materially from those discussed in the forward-looking statements: technological advances by the Company's competitors, changes in health care reform, including reimbursement programs, changes to regulatory requirements relating to environmental approvals for the treatment of infectious medical waste, capital

11

needs to fund any delays or extensions of development programs, delays in the manufacture of new and existing products by the Company or third party contractors, the loss of any key employees, the outcome of existing litigations, delays in obtaining federal, state or local regulatory clearance for new installations and operations, changes in governmental regulations, the location of the MCM business in Israel, and availability of capital on terms satisfactory to the Company. The Company is also subject to numerous Risk Factors relating to manufacturing, regulatory, financial resources and personnel as defined in the Company's September 30, 2004 Form 10KSB as filed with the Securities and Exchange Commission. The Company disclaims any obligation to update any forward-looking statements to reflect events or circumstances after the date hereof.

RESULTS OF OPERATIONS

As more fully described in the Form 10-KSB for fiscal year ended September 30, 2004, the Company's continuing operation is classified as medical infectious waste business.

THREE MONTHS DECEMBER 31, 2004 COMPARED TO THREE MONTHS ENDED DECEMBER 31, 2003

Edgar Filing: CAPRIUS INC - Form 10QSB

Revenues generated from MCM product sales totaled \$236,908 for the three months ended December 31, 2004 as compared to \$258,884 for the three months ended December 31, 2003. Revenues generated from MCM rentals totaled \$5,326 as compared to \$18,349 for the comparable periods. Consulting and royalty income totaled \$20,425 as compared to \$12,500 for the three months ended December 31, 2004 and 2003 in connection with the sale of the TDM Business.

Cost of product sales and leased equipment amounted to \$161,794 or 61.6% of total revenues versus \$204,719 or 70.1% of total revenues for the three month period ended December 31, 2004 and 2003, respectively. The Company has not advanced to a level of sales for the Company to fully absorb the fixed costs related to its revenues.

Selling, general and administrative expenses totaled \$672,278 for the three months ended December 31, 2004 versus \$674,236 for the three months ended December 31, 2003.

Interest expense, net totaled \$149,079 for the three months ended December 31, 2004 versus \$434 for the three months ended December 31, 2003. The majority of the interest expense incurred during the three month period ended December 31, 2004, related to interest fees and amortization in connection with the secured convertible notes and bridge financing, which occurred in Fiscal 2004.

The operating loss from operations amounted to \$647,993 and \$628,817 for the three month periods ended December 31, 2004 and 2003, respectively.

LIQUIDITY AND CAPITAL RESOURCES

At December 31, 2004, the Company's cash and cash equivalents position approximated \$19,100 versus \$27,600 at September 30, 2004. As further discussed below, on February 15, 2005 the Company received gross proceeds of \$4.5 million, under a preferred stock equity financing.

During the three month period ended December 31, 2004, the Company was advanced the principal amount of approximately \$138,800 through short-term related party loans until additional equity funding was secured. The terms of the loans are identical to the terms of the \$100,000 8% Senior Secured Convertible Promissory Note outlined in Note 9. These funds were utilized for general working capital purposes. These loans were repaid on February 15, 2005 as part of the Preferred Stock Equity Financing arrangement.

On February 2, 2005, the Company raised \$100,000 through the issuance of an 8% Senior Secured Convertible Promissory Note, due April 3, 2005, subject to repayment in the event of an equity financing in excess of \$2 million or conversion by the investors to shares of our common stock at \$ 0.15 per share. Thus loan was repaid on February 15, 2005 as part of the Preferred Stock Equity Financing arrangement.

On February 15, 2005, the Company closed on a \$4.5 million preferred stock equity financing, before financing related fees and expenses of approximately 10% (see Note 9). As part of this financing, the Company agreed to 30% warrant coverage for the purchase of common stock at an exercise price of \$0.28 per share for a period of five years. The Company also agreed to a second warrant with 10% coverage for the purchase of common stock at \$0.145 per share for a period of five years exercisable after 9 months. Simultaneously, the Company

Edgar Filing: CAPRIUS INC - Form 10QSB

converted the short-term secured debt outstanding in the aggregate of \$2 million together with \$72,962 into 21,681 shares of Series C Mandatory Convertible Preferred Stock as the new equity investors. As part of the condition for raising the equity financing, holders of a majority of the outstanding shares irrevocably undertook to effect a 1:20 reverse stock split of any outstanding shares of common stock. At the time that the reverse split becomes effective, all of the preferred stock issued to the new equity investors and the debt holders who converted their debt will automatically convert into common shares. Additionally, the holders of the \$1.5 million 8% Senior Secured Convertible Promissory Notes, exchanged their indebtedness for 15,953 shares of Series C Mandatory Convertible Preferred Stock. Further, the Company satisfied the related party debt with a combination of 5,728 shares of Series C Mandatory Convertible Preferred Stock and cash consideration. In addition certain accounts payable and accrued expenses were required to be paid as defined under the Agreement. The Company also agreed to increase the number of independent directors by one additional director and obtain a listing on the Nasdaq Small Cap Market. The net cash proceeds from the equity financing will provide the funds necessary to expand our business as well as meeting our needs to satisfy specific outstanding obligations and accrued expenses. Specifically, the funds will be used to increase our marketing effort both in the US and overseas markets. The availability of this working capital will also permit us to build inventory to fulfill both current and future needs arising from our increased marketing efforts. In addition, as we start to build a meaningful penetration in the US market, we will need to expand our customer service and technical support capabilities to meet the needs of our clients. Similarly, in overseas markets, resources will be required to obtain regulatory approvals in markets where we believe there exists great opportunities for its business. We may also use our resources to develop further versions of our SteriMed System if it is determined that there is a market for such a product.

The Company has for the past several years met its need for capital in its various businesses through loans from officers, directors and related parties other than the monies received from the sale of the TDM business, which were primarily used to finance the acquired MCM business on December 17, 2002.

CRITICAL ACCOUNTING POLICIES

The preparation of financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues, expenses and related disclosures. On an on-going basis, management evaluates our estimates and assumptions, including but not limited to those related to revenue recognition and the impairment of long-lived assets, goodwill and other intangible assets. Management bases its estimates on historical experience and various other assumptions that it believes to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

1. Revenue recognition

The infectious medical waste business recognizes revenues from either the sale or rental of our SteriMed Systems. Revenues for sales are recognized at the time that the unit is shipped to the customer. Rental revenues are recognized based upon either services provided for each month of activity or evenly over the year in the event that a fixed rental agreement is in place.

2. Goodwill and other intangibles

Goodwill and other intangibles associated with the MCM acquisition will be subject to an annual assessment for impairment by applying a fair-value based test. The valuation will be based upon estimates of future income of the

Edgar Filing: CAPRIUS INC - Form 10QSB

reporting unit and estimates of the market value of the unit.

13

ITEM 3. CONTROLS & PROCEDURES

The Company's principal executive officer and principal financial officer, based on their evaluation of the Company's disclosure controls and procedures (as defined in Rules 13a-14 (c) and 15d-14 (c) of the Securities Exchange Act of 1934) as of December 31, 2004 have concluded that the Company's disclosure controls and procedures are adequate and effective to ensure that material information relating to the Company and its consolidated subsidiaries are recorded, processed, summarized and reported within the time periods specified by the SEC's rules and forms, particularly during the period in which this quarterly report has been prepared.

The Company's principal executive officer and principal financial officer have concluded that there were no significant changes in the Company's internal controls or in other factors that could significantly affect these controls for the quarter ended December 31, 2004, the date of their most recent evaluation of such controls, and that there were no significant deficiencies or material weaknesses in the Company's internal controls.

PART II: OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

In June 2002, Jack Nelson, a former Caprius executive officer and director, commenced two legal proceedings against us and George Aaron and Jonathan Joels, executive officers, directors and principal stockholders. The two complaints alleged that the individual defendants made misrepresentations to the plaintiff upon their acquisition of a controlling interest in the Company in 1999 and thereafter made other alleged misrepresentations and engaged in mismanagement and other misconduct and took other actions as to the plaintiff to the supposed detriment of the plaintiff and Caprius. One action was brought in Superior Court of New Jersey, Bergen County ("State Court Action"), and the other was brought as a derivative action in Federal District Court in New Jersey ("Federal Derivative Action"). In September 2003, we resolved the State Court Action by making an Offer of Judgment which was accepted by the plaintiff. Under the terms of the Offer of Judgment, which was made without any admission or finding of liability on part of the defendants, we paid \$125,000 to the plaintiff and the action was discontinued.

On May 3, 2004, the Court in the Federal Derivative Action granted the motion made by us and Messrs. Aaron and Joels for judgment on the pleadings based upon the pre-suit demand requirement and dismissed the plaintiff's complaint without prejudice, but denied defendants' motion for judgment on the pleadings based upon the Private Securities Litigation Reform Act. The Court also granted the plaintiff's cross-motion to file an amended complaint to add allegations of insider trading.

In September 2002, we were served with a complaint naming us and our principal officers and directors in the Federal District Court of New Jersey as a purported class action (the "Class Action"). The allegations in the complaint cover the period between February 14, 2000 and June 20, 2002. The initial plaintiff is a relative of the wife of the plaintiff in the State Court Action and Federal Derivative Action. The allegations in the purported Class Action were substantially similar to those in the other two Actions. The complaint sought an unspecified amount of monetary damages, as well as the removal of the

Edgar Filing: CAPRIUS INC - Form 10QSB

defendant officers as shareholders.

On May 3, 2004, in a decision separate from the decision in the Federal Derivative Action, the Court granted the defendants' motion and dismissed the Class Action. The federal securities claims asserted by the plaintiffs were dismissed with prejudice, and having dismissed all federal law claims, the Court declined to exercise jurisdiction over the remaining state law claims and dismissed those claims without prejudice. On May 14, 2004, the plaintiffs filed a motion for reconsideration, which defendants opposed and subsequently this motion for reargument was denied. The plaintiff did not file a notice of appeal during the statutory time period.

On September 30, 2004, our Board received a letter written from Mr. Nelson's attorney making a demand that we institute a derivative action substantially similar to the allegations presented in the Federal Derivative Action. A draft complaint was included with the letter. An Independent Committee of the Board responded to the letter within the stipulated 90 day period that

14

Mr. Nelson had requested, stating that the Independent Committee determined that there was no basis for the Company to institute the derivative action as demanded. There has been no further communication from Mr. Nelson's attorney.

The independent directors have authorized us to advance the legal expenses of Messrs. Aaron and Joels in these litigations with respect to claims against them in their corporate capacities, subject to review of the legal bills and compliance with applicable law, and Messrs. Aaron and Joels will repay us in the event it was determined that they were not entitled to be indemnified as to the claim for which the advance was made.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

- 3.1 Certificate of Designations, Preferences and Rights of Series C Mandatory Convertible Preferred Stock (incorporated by reference to Exhibit 3.1 to Registrant's Form 8-K filed for an event of February 15, 2005)
- 4.1 Form of Series A Warrant (granted February 15, 2005) (incorporated by reference to Exhibit 4.1 to Registrant's Form 8-K filed for an event of February 15, 2005).
- 4.2 Form of Series B Warrant (granted February 15, 2005) (incorporated by reference to Exhibit 4.2 to Registrant's Form 8-K filed for an event of February 15, 2005).
- 4.3 Form of Dealer Warrant (granted February 15, 2005) (incorporated by reference to Exhibit 4.3 to Registrant's Form 8-K filed for an event of February 15, 2005).
- 4.4 Form of Lock-Up Agreement with George Aaron and Jonathan Joels (incorporated by reference to Exhibit 4.4 to Registrant's Form 8-K filed for an event of February 15, 2005).
- 10.1 Purchase Agreement for the sale of 45,000 shares of Series C

Edgar Filing: CAPRIUS INC - Form 10QSB

Mandatory Convertible Preferred Stock and Series A and Series B warrants (incorporated by reference to Exhibit 10.1 to Registrant's Form 8-K filed for an event of February 15, 2005).

- 10.2 Registration Rights Agreement, dated February 15, 2005, by and among the Registrant and note holders (incorporated by reference to Exhibit 10.2 to Registrant's Form 8-K filed for an event of February 15, 2005).
- 10.3 Amendment and Conversion Agreement, dated February 15, 2005, by and among the Registrant and note holders (incorporated by reference to Exhibit 10.3 to Registrant's Form 8-K filed for an event of February 15, 2005).
- 10.4 Exchange Agreement, dated February 15, 2005, by and among the Registrant and certain lenders (incorporated by reference to Exhibit 10.4 to Registrant's Form 8-K filed for an event of February 15, 2005).
- 10.5 Registration Rights Agreement, dated February 15, 2005, by and among the Registrant and note holders (incorporated by reference to Exhibit 10.5 to Registrant's Form 8-K filed for an event of February 15, 2005).
- 10.6.1 Financial Advisory Agreement, dated January 11, 2005, between the Registrant and Laidlaw & Company (UK) Ltd. (incorporated by reference to Exhibit 10.6.1 to Registrant's Form 8-K filed for an event of February 15, 2005).

15

- 10.6.2 Amendment to Financial Advisory Agreement, dated February 9, 2005 (incorporated by reference to Exhibit 10.6.2 to Registrant's Form 8-K filed for an event of February 15, 2005).
- 31.1* Rule 13a-14(a)/15d-14(a) Certification
- 31.2* Rule 13a-14(a)/15d-14(a) Certification
- 32* Section 1350 - Certification

* filed herewith

(b) Reports on Form 8-K:

None

16

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.

Edgar Filing: CAPRIUS INC - Form 10QSB

Caprius, Inc.

(Registrant)

Date: February 22, 2005

/s/ George Aaron

George Aaron
President & Chief Executive Officer

Date: February 22, 2005

/s/ Jonathan Joels

Jonathan Joels
Chief Financial Officer