Parametric Sound Corp
Form 10-Q
January 25, 2011

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

FORM 10-Q

(Mark one)
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended December 31, 2010
Commission File Number: 000-54020

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

Nevada (State or other jurisdiction of incorporation or organization)	27-2767540 (I.R.S. Employer Identification Number)
1941 Ramrod Avenue, Suite #100 Henderson, Nevada 89014 (Address of principal executive offices)	89014 (Zip Code)

(888) 477-2150
(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 x 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 o 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.

Large accelerated filer ¨ Accelerated filer ¨ Non-accelerated filer ¨

	Smaller reporting company x
(Do not check if a smaller reporting company)	

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

The number of shares of Common Stock, $0.001 par value, outstanding on January 24, 2011 was 15,306,064.

PARAMETRIC SOUND CORPORATION

INDEX

PART I. FINANCIAL INFORMATION

Item 1 - Financial Statements

Parametric Sound Corporation
Condensed Balance Sheets

	December 31, 2010 (unaudited)	September 30, 2010
ASSETS		
Current assets:		
Cash	$215,844	$439,385
Inventories, net	206	206
Prepaid expenses and other current assets	19,985	20,779
Total current assets	236,035	460,370
Equipment and tooling, net	17,040	8,091
Patents and trademarks, net	151,166	175,726
Total assets	$404,241	$644,187
LIABILITIES AND STOCKHOLDERS' (DEFICIT) EQUITY		
Current liabilities:		
Accounts payable	$99,620	$147,670
Accrued liabilities	66,922	27,307
Subordinated notes payable, net of discount of $207,818 and $263,272, respectively	492,182	436,728
Total current liabilities	658,724	611,705
Commitments and contingencies (Note 7)		
Stockholders' (deficit) equity:		
Preferred stock, $0.001 par value, authorized 1,000,000 shares, none issued and outstanding	-	-
Common stock, $0.001 par value, authorized 50,000,000 shares, 15,306,064 shares issued and outstanding each period	15,306	15,306
Additional paid-in capital	742,102	703,127
Accumulated deficit	(1,011,891)	(685,951)
Total stockholders' (deficit) equity	(254,483)	32,482
Total liabilities and stockholders' (deficit) equity	$404,241	$644,187

See accompanying notes to financial statements

Parametric Sound Corporation
Condensed Statements of Operations

	Three Months Ended December 31, 2010	2009
Revenues:		
Product sales	$-	$93,617
Other revenue	-	2,185
Total revenues	-	95,802
Cost of revenues	-	72,350
Gross profit	-	23,452
Operating expenses:		
Selling, general and administrative	129,344	43,870
Research and development	112,155	16,959
Patent impairment	14,242	20,801
Total operating expenses	255,741	81,630
Loss from operations	(255,741)	(58,178)
Other income (expense):		
Interest and note discount amortization	(70,276)	-
Other	77	-
	(70,199)	-
Net loss	$(325,940)	$(58,178)
Loss per basic and diluted share	$(0.02)	$(0.00)
Weighted average shares used to compute net loss per basic and diluted share	15,306,064	15,306,064

See accompanying notes to financial statements

Parametric Sound Corporation
Condensed Statements of Cash Flows

	Three Months Ended December 31, 2010	2009
Decrease in Cash and Cash Equivalents:		
Operating Activities:		
Net loss	$(325,940)	$(58,178)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	11,310	16,959
Debt discount and deferred financing cost amortization	56,161	-
Share-based compensation	38,975	2,467
Impairment of patents	14,242	20,801
Changes in assets and liabilities:		
Accounts receivable	-	18,615
Prepaid expenses and other current assets	87	-
Inventories	-	56,004
Accounts payable	(48,050)	(1,890)
Accrued liabilities	39,615	(35,343)
Net cash provided (used in) by operating activities	(213,600)	19,435
Investing Activities:		
Capital expenditures for equipment	(9,941)	-
Patent costs paid	-	(3,240)
Net cash used in investing activities	(9,941)	(3,240)
Financing Activities:		
Net change in investment from LRAD Corporation	-	(16,195)
Net cash used in financing activities	-	(16,195)
Net decrease in cash and cash equivalents	(223,541)	-
Cash and cash equivalents, beginning of period	439,385	-
Cash and cash equivalents, end of period	$215,844	$-

See accompanying notes to financial statements

Parametric Sound Corporation
Notes to Interim Condensed Financial Statements
(unaudited)
December 31, 2010

Note 1 - Description of Business and Basis of Accounting/Presentation

In April 2010, the board of directors of LRAD Corporation approved a plan to separate its HyperSonic Sound ("HSS") product line into a new independent, stand-alone company. In a special meeting of stockholders held June 2, 2010, the proposal to separate the HSS business from LRAD Corporation was approved, and on June 2, 2010, LRAD Corporation created a new wholly owned subsidiary, Parametric Sound Corporation ("Parametric Sound" or the "Company"), into which the HSS business and substantially all of the assets of the business and associated intellectual property rights were contributed.

The distribution of 100% of the Parametric Sound common stock to the stockholders of LRAD Corporation occurred on September 27, 2010, at a ratio of one share of Parametric Sound common stock for each two shares of LRAD Corporation common stock held by each such holder as of the record date of September 10, 2010 ("Spin-Off"). Following the Spin-Off the common stock of the Company commenced trading and quotation on the OTCBB under the symbol "PAMT". LRAD Corporation no longer has any ownership or other form of interest in Parametric Sound.

In connection with the separation, Parametric Sound and LRAD Corporation entered into a separation agreement and a tax sharing agreement. See Note 2 for further discussion regarding these agreements.

Parametric Sound's HSS technology consists of proprietary parametric sound technology that generates audible sound along an air column using ultrasonic frequencies above the normal range of hearing. HSS products are compatible with standard media sources and the highly directional sound beam localizes or shines sound where intended by users. The Company is developing a new HSS product line for which sales have not yet commenced and has no plans to sell the product line previously sold by LRAD Corporation. The Company's corporate headquarters are located in Henderson, Nevada and new product development is performed in San Diego, California. Principal markets are expected to be in North America, Europe and Asia.

Basis of Accounting

The accompanying unaudited interim financial statements have been prepared by the Company in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial information and pursuant to the applicable rules and regulations of the Securities and Exchange Commission. In the opinion of management, the accompanying financial statements contain all adjustments (consisting of normal and recurring accruals) necessary in order make the financial statements not misleading. The condensed balance sheet as of September 30, 2010 was derived from the Company's most recent audited financial statements. The financial statements herein should be read in conjunction with the Company's audited financial statements and notes thereto for the fiscal year ended September 30, 2010, included in the Company's Annual Report on Form 10-K for the year ended September 30, 2010. Operating results for the three months ended December 31, 2010 may not necessarily be indicative of results to be expected for any other interim period or for the full year.

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements, as well as the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The Company's balance sheet as of September 30, 2010, reflect the opening balances of Parametric Sound as an independent company on September 27, 2010 adjusted for separate company activity through September 30, 2010 including certain start-up, spin-off and technology costs incurred on the Company's behalf prior to the spin-off. The Company's financial statements for the three months ended December 31, 2009 were derived from LRAD Corporation's historical consolidated financial statements using LRAD Corporation's historical costs basis of assets and liabilities of the various activities that reflect the results of operations, financial condition and cash flows of Parametric Sound as a component of LRAD Corporation. Historically, the HSS business in LRAD Corporation operated as a product line and not a separate segment and not as an independent stand-alone business. For purposes of preparing the financial statements in the year prior to the September 27, 2010 separation, Parametric Sound was allocated certain expenses from LRAD Corporation with such expenses reflected in the statements of operations as expense allocations from LRAD Corporation. Management believes that the assumptions and allocation methods underlying such prior year financial statements are reasonable in all material respects. However, the costs allocated to the Company are not necessarily indicative of the costs that would have been incurred if the Company operated as a stand-alone entity during the three months ended December 31, 2009.

Parametric Sound Corporation
Notes to Interim Condensed Financial Statements
(unaudited)
December 31, 2010

Liquidity/Going Concern

The financial statements have been prepared on a going concern basis contemplating the realization of assets and the satisfaction of liabilities in the normal course of business. The Company had a net loss of $325,940 for the three months ended December 31, 2010 and as of December 31, 2010 had current liabilities of $658,724, presented net of unamortized debt discount in the amount of $207,818, in excess of current assets by $422,689. The Company obtained proceeds of $450,000 through the issuance of subordinated notes payable on September 28, 2010, and which are due on September 28, 2011, with an aggregate principal balance of $700,000 (see Note 5). The Company has no other sources of financing available as of December 31, 2010. The Company does not plan to continue to sell the HSS product models previously sold by LRAD Corporation and plans to introduce a new product line currently under development. Accordingly historical revenues are no indication of future revenues and there can be no assurance that Parametric Sound will be successful in introducing a new product line or that it will achieve any market success. The Company will be reliant on existing or additional debt or equity financing sufficient to sustain operations until profitability can be achieved.

The continuation of the Company as a going concern is dependent on its ability to develop revenues and to obtain additional financing from outside sources. There is no assurance that the Company will be successful in generating or raising funds to sustain its operations for twelve months or beyond. Should the Company be unable to obtain required financing, it may have to curtail operations, which may have a material adverse effect on its financial position and results of operations. The accompanying financial statements do not include any adjustments that would be necessary should the Company be unable to continue as a going concern and, therefore, be required to liquidate its assets and discharge its liabilities in other than the normal course of business and at amounts different from those reflected in the accompanying financial statements.

Reclassifications

Where necessary, the prior year’s information has been reclassified to conform to the current period’s statement presentation.

Loss Per Share

Basic loss per common share is computed by dividing net loss by the weighted-average number of shares of common stock outstanding during the period. Diluted net loss per share reflects the potential dilution of securities that could share in the earnings of an entity. The Company’s losses for the periods presented cause the inclusion of potential common stock instruments outstanding to be antidilutive. Stock options and warrants exercisable for 2,955,000 shares of common stock were outstanding at December 31, 2010. These securities are not included in the computation of diluted net loss per share because of the losses, but could potentially dilute earnings per share in future periods.

For the prior year period ended December 31, 2009 the pro forma net loss per basic and diluted share and the weighted-average shares outstanding were calculated based on the 15,306,064 shares issued in connection with the Spin-Off.

Recent Accounting Pronouncements

The Company reviews new accounting standards as issued. Although some of these accounting standards issued or effective after the end of the Company's previous fiscal year may be applicable to the Company, it has not identified any standards that it believes merit further discussion. The Company believes that none of the new standards will have a significant impact on its financial statements.

Parametric Sound Corporation
Notes to Interim Condensed Financial Statements
(unaudited)
December 31, 2010

Note 2 - Spin-Off of HSS Business

On September 27, 2010, LRAD Corporation separated its HSS business through the Spin-Off of Parametric Sound. LRAD Corporation contributed most of its HSS business assets to Parametric Sound. All outstanding shares of the Company were then distributed to LRAD Corporation's stockholders of record at the close of business on September 10, 2010 as a pro-rata, tax-free dividend of one share of Parametric Sound common stock for every two shares of LRAD Corporation's common stock.

On September 27, 2010, the Company entered into a Separation and Distribution Agreement ("Separation Agreement") with LRAD Corporation that set forth the terms and conditions of the separation of the Company from LRAD Corporation, provides the framework for the relationship between the Company and LRAD Corporation following the separation and provided for the allocation of assets, liabilities and obligations between the Company and LRAD Corporation in connection with the separation. The Separation Agreement also provided for a transition related to HSS business and customers with LRAD Corporation fulfilling any orders received through September 27, 2010. Thereafter LRAD Corporation may fulfill any continuing purchase orders for a current project with customer Cardinal Health through the completion of such project and may accept unsolicited follow-on orders for existing HSS products from current customers through December 31, 2010. LRAD Corporation retained inventory and supplies to fulfill anticipated orders and is responsible for warranty, returns and related liabilities for such customers and sales. On September 27, 2010 the Company also entered into a Tax Sharing Agreement with LRAD Corporation that generally governs the parties' respective rights, responsibilities and obligations after the separation with respect to taxes.

On September 27, 2010, the Company entered into a License and Royalty Agreement with related party Syzygy Licensing LLC ("Syzygy") relating to new technology invented by the Company's CEO, Elwood G. Norris. This technology is being implemented in the Company's planned line of directed sound products. The Company also assumed and became obligated on a lease for 4,500 square feet of office, testing, assembly and warehousing space at 1941 Ramrod Avenue, Suite #100, Henderson, Nevada 89014, pursuant to a lease at a net monthly rate of $2,000 (gross $4,000 and a sublease for certain unused space at $2,000 per month) expiring June 30, 2011.

The total value of the LRAD Corporation stock dividend of $454,006 was based on the net book value of the net assets that were transferred from LRAD Corporation in connection with the Spin-Off in accordance with ASC 845-10-30-10, Nonreciprocal Transfers with Owners.

Note 3 - Patents and Trademarks, net

Patents and trademarks consist of the following:

	December 31, 2010	September 30, 2010
Patents	$ 108,103	$ 127,771
Defensive patents	222,017	222,017
Trademarks	6,292	6,292
	336,412	356,080
Accumulated amortization	(185,246)	(180,354)
	$ 151,166	$ 175,726

Aggregate amortization expense for the Company's patents and trademarks was $10,161 and $16,959 during the three months ended December 31, 2010 and 2009, respectively. In addition to amortization, the Company wrote off $14,242 and $20,801 of impaired patent costs during the three months ended December 31, 2010 and 2009, respectively.

Parametric Sound Corporation
Notes to Interim Condensed Financial Statements
(unaudited)
December 31, 2010

Note 4 - Accrued Liabilities

Accrued liabilities consisted of the following:

		December 31, 2010		September 30, 2010
Accrued officer compensation	$	52,500	$	-
Accrued interest		14,422		307
Other		-		27,000
	$	66,922	$	27,307

Note 5 - Subordinated Notes Payable and Warrants

In September 2010 the Company sold $700,000 of 8% Subordinated Promissory Notes, due September 28, 2011 (the “Notes”), and accompanying warrants to purchase an aggregate of 1,400,000 shares of common stock (“Warrants”). The Notes are subordinate to any senior debt so designated from time to time by the Board of Directors. The Company capitalized in other current assets $2,766 of costs directly related to the financing and amortizes these costs as additional interest expense over the terms of the related debt. Amortization for the period ended December 31, 2010 was $707. The accrued interest related to notes payable at December 31, 2010 totaled $14,422 and is included in accrued liabilities.

The Warrants are exercisable at $0.30 per common share until September 28, 2015 and include a cashless exercise provision, subject to the Company’s right to first offset any exercise proceeds as a reduction of the Notes. The Warrants are callable at the Company’s option if for any period of ten consecutive trading days the closing price exceeds $0.90 per share.

The fair value of the Warrants of $264,427 was recorded as a note discount and is being amortized as additional interest expense using the effective interest method over the term of the Notes with $55,454 amortized during the three months ended December 31, 2010. The net unamortized note discount balance was $207,818 at December 31, 2010.

A total of $260,000 of the Notes are held by Syzygy and an additional $100,000 are held by an entity owned by our CEO, Mr. Norris. Interest accrued for such related party holders during the three months ended December 31, 2010 was $7,259 with the aggregate accrued interest liability to such holders being $7,417 at December 31, 2010.

Note 6 - Share-Based Compensation

Pursuant to LRAD Corporation’s 2005 Equity Incentive Plan, the Company recorded $2,467 of stock compensation expense for the three months ended December 31, 2009 related to personnel whose salary and benefit costs were allocated to the Company. No stock options were granted to such allocated personnel during fiscal 2009 and no legacy options were outstanding at the Spin-Off.

On September 27, 2010 the Company adopted the 2010 Stock Option Plan (the “2010 Plan”). The 2010 Plan authorizes the grant of options to purchase up to 3,000,000 shares of the Company’s common stock to directors, officers, employees and consultants. During the three months ended December 31, 2010 the Company granted options on 1,555,000 shares of common stock vesting quarterly over two years, subject to the terms of the 2010 Plan. The Company’s stock options have various restrictions that reduce option value, including vesting provisions and restrictions on transfer, among others, and may be exercised prior to their contractual maturity.

Parametric Sound Corporation
Notes to Interim Condensed Financial Statements
(unaudited)
December 31, 2010

The Company accounts for stock-based compensation under the provisions of ASC 718, Share-Based Payment and ASC 505-50, Equity-Based Payments to Non-Employees. ASC 718 requires measurement of all employee stock-based awards using a fair-value method and recording of related compensation expense in the financial statements over the requisite service period. Further, as required under ASC 718, the Company estimates forfeitures for stock-based awards that are not expected to vest. The Company uses the Black-Scholes option pricing model to determine the estimated fair value of each option asof its grant date. These inputs are subjective and generally require significant analysis and judgment to develop. The following table sets forth the significant assumptions used in the Black-Scholes model and the calculation of stock-based compensation cost (annualized percentages):

Years Ended September 30,	Three Months Ended December 31, 2010
Volatility	100%
Risk-free interest rate	1.06%
Forfeiture rate	0.00%
Dividend yield	0.00%
Expected life in years	4.75
Weighted average fair value of options granted	$0.22

Since the Company's stock has only recently commenced trading, the Company's management estimated its expected volatility by reviewing the historical volatility of the common stock of a group of selected peer public companies that operate in similar industries and are similar in terms of stage of development or size and then projecting this information toward its future expected results. Judgment was used in selecting these companies, as well as in evaluating the available historical volatility for these peer companies. The risk-free interest rate is based on rates published by the Federal Reserve Board. The dividend yield of zero is based on the fact that the Company has never paid cash dividends and has no present intention to pay cash dividends. The Company has a small number of option grants and no exercise history and accordingly has for all new option grants applied the simplified method prescribed by SEC Staff Accounting Bulletin 110, Share-Based Payment: Certain Assumptions Used in Valuation Methods - Expected Term, to estimate expected life (computed as vesting term plus contractual term divided by two). An estimated forfeiture rate was determined to be zero as the number of grantees is limited and all are currently expected to serve in their capacities during the vesting period. Forfeitures are estimated at the time of the grant and revised in subsequent periods if actual forfeitures differ from those estimates or if the Company updates its estimated forfeiture rate. Such amounts will be recorded as a cumulative adjustment in the period in which the estimate is changed.

The Company recorded stock-based compensation in its statements of operations for the relevant periods as follows:

	Three Months Ended December 31,			
		2010		2009
Cost of revenue	$	-	$	388
Selling, general and administrative		19,594		2,079
Research and development		19,381		-
	$	38,975	$	2,467

As of December 31, 2010 total estimated compensation cost relating to stock options granted but not yet vested was $299,124. This cost is expected to be recognized over the weighted average period of 1.8 years.

Parametric Sound Corporation
Notes to Interim Condensed Financial Statements
(unaudited)
December 31, 2010

The following table summarizes stock option activity for the period: