

Akeena Solar, Inc.
Form 10-Q
May 04, 2009

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-Q

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended March 31, 2009

or

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from _____ to _____

Commission File Number 001-33695

AKEENA SOLAR, INC.
(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

90-0181035
(I.R.S. Employer Identification No.)

16005 Los Gatos Boulevard, Los Gatos, CA
(Address of principal executive offices)

95032
(Zip Code)

(408) 402-9400

(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 No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company)

Smaller reporting company

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

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As of April 29, 2009, 32,083,459 shares of the issuer's common stock, par value \$0.001 per share, were outstanding (including non-vested restricted shares).

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements.

AKEENA SOLAR, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

| | (Unaudited) March 31, 2009 | December 31, 2008 |
|--|----------------------------------|----------------------|
| Assets | | |
| Current assets | | |
| Cash and cash equivalents | \$ 2,864,708 | \$ 148,230 |
| Restricted cash | — | 17,500,000 |
| Accounts receivable, net | 5,390,104 | 7,660,039 |
| Other receivables | 302,117 | 331,057 |
| Inventory, net | 7,093,191 | 10,495,572 |
| Prepaid expenses and other current assets, net | 2,216,624 | 3,704,375 |
| Total current assets | 17,866,744 | 39,839,273 |
| Property and equipment, net | 1,630,046 | 1,806,269 |
| Goodwill | 298,500 | 298,500 |
| Other assets, net | 192,627 | 194,346 |
| Total assets | \$ 19,987,917 | \$ 42,138,388 |
| Liabilities and Stockholders' Equity | | |
| Current liabilities | | |
| Accounts payable | \$ 1,004,759 | \$ 1,922,480 |
| Customer rebate payable | 282,825 | 271,121 |
| Accrued liabilities | 1,742,545 | 2,410,332 |
| Accrued warranty | 1,116,548 | 1,056,655 |
| Common stock warrant liability | 3,043,112 | — |
| Deferred revenue | 779,069 | 1,057,941 |
| Credit facility | — | 18,746,439 |
| Current portion of capital lease obligations | 22,094 | 23,292 |
| Current portion of vehicle loans | 215,457 | 219,876 |
| Total current liabilities | 8,206,409 | 25,708,136 |
| Capital lease obligations, less current portion | 18,393 | 20,617 |
| Vehicle loans, less current portion | 483,098 | 535,302 |
| Other long-term liabilities | 63,164 | — |
| Total liabilities | 8,771,064 | 26,264,055 |
| Commitments, contingencies and subsequent events (Notes 14 and 15) | | |
| Stockholders' equity: | | |
| Common stock, \$0.001 par value; 50,000,000 shares authorized; 30,820,744 and 28,460,837 shares issued and outstanding at March 31, 2009 and December 31, 2008, respectively | 30,820 | 28,460 |
| Additional paid-in capital | 52,242,045 | 52,821,104 |
| Accumulated deficit | (41,056,012) | (36,975,231) |
| Total stockholders' equity | 11,216,853 | 15,874,333 |
| Total liabilities and stockholders' equity | \$ 19,987,917 | \$ 42,138,388 |

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

AKEENA SOLAR, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

| | Three Months Ended March 31, | |
|--|------------------------------|----------------|
| | 2009 | 2008 |
| Net sales | \$ 7,594,590 | \$ 12,248,372 |
| Cost of sales | 5,339,982 | 9,832,817 |
| Gross profit | 2,254,608 | 2,415,555 |
| Operating expenses | | |
| Sales and marketing | 1,654,121 | 2,116,294 |
| General and administrative | 4,061,406 | 5,012,357 |
| Total operating expenses | 5,715,527 | 7,128,651 |
| Loss from operations | (3,460,919) | (4,713,096) |
| Other income (expense) | | |
| Interest income (expense), net | (76,541) | 134,939 |
| Adjustment to the fair value of common stock warrants | (1,541,764) | — |
| Total other income (expense) | (1,618,305) | 134,939 |
| Loss before provision for income taxes | (5,079,224) | (4,578,157) |
| Provision for income taxes | — | — |
| Net loss | \$ (5,079,224) | \$ (4,578,157) |
| | | |
| Loss per common and common equivalent share: | | |
| Basic | \$ (0.17) | \$ (0.16) |
| Diluted | \$ (0.17) | \$ (0.16) |
| Weighted average shares used in computing loss per common and common equivalent share: | | |
| Basic | 29,183,603 | 27,760,194 |
| Diluted | 29,183,603 | 27,760,194 |

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

AKEENA SOLAR, INC.
 CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
 (Unaudited)

| | Common Stock | | Additional | Accumulated | Stockholders' |
|--|--------------|-----------|---------------|-----------------|---------------|
| | Number | Amount | Paid-in | Deficit | Equity |
| | of Shares | | Capital | | |
| Balance at January 1, 2009 | 28,460,837 | \$ 28,460 | \$ 52,821,104 | \$ (36,975,231) | \$ 15,874,333 |
| Cumulative effect of reclassification of warrants (EITF 07-05) | — | — | (1,287,795) | 998,443 | (289,352) |
| Balance at January 1, 2009, as adjusted | 28,460,837 | 28,460 | 51,533,309 | (35,976,788) | 15,584,981 |
| Issuance of common shares pursuant to stock offering | 1,785,714 | 1,786 | 1,381,086 | — | 1,382,872 |
| Fair value of warrants issued in connection with stock offering | — | — | (1,676,282) | — | (1,676,282) |
| Conversion of preferred stock issued in connection with stock offering | 539,867 | 540 | 463,746 | — | 464,286 |
| Release of restricted common shares and stock-based compensation expense | 34,326 | 34 | 540,186 | — | 540,220 |
| Net loss | — | — | — | (5,079,224) | (5,079,224) |
| Balance at March 31, 2009 | 30,820,744 | \$ 30,820 | \$ 52,242,045 | \$ (41,056,012) | \$ 11,216,853 |

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

AKEENA SOLAR, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

| | Three Months Ended March 31, | |
|---|------------------------------|----------------|
| | 2009 | 2008 |
| Cash flows from operating activities | | |
| Net loss | \$ (5,079,224) | \$ (4,578,157) |
| Adjustments to reconcile net loss to net cash used in operations | | |
| Depreciation | 176,223 | 126,743 |
| Amortization of customer list, customer contracts and patents | 1,236 | 113,163 |
| Bad debt expense | 104,575 | 33,646 |
| Fair value adjustment of common stock warrants | 1,541,764 | — |
| Non-cash stock-based compensation expense | 540,220 | 1,016,359 |
| Changes in assets and liabilities: | | |
| Accounts receivable | 2,165,360 | (2,387,348) |
| Other receivables | 28,940 | 13,747 |
| Inventory | 3,402,381 | 767,244 |
| Prepaid expenses and other current assets | 1,487,751 | (829,673) |
| Other assets | 483 | (52,835) |
| Accounts payable | (917,721) | (3,210,507) |
| Customer rebate payable | 11,704 | (6,203) |
| Accrued liabilities and accrued warranty | (607,894) | 1,982,979 |
| Other long-term liabilities | 63,164 | — |
| Deferred revenue | (278,872) | (151,430) |
| Net cash provided by (used in) operating activities | 2,640,090 | (7,162,272) |
| Cash flows from investing activities | | |
| Acquisition of property and equipment | — | (218,599) |
| Net cash used in investing activities | — | (218,599) |
| Cash flows from financing activities | | |
| Repayment of vehicle loans | (56,623) | (46,540) |
| Borrowings (repayments) on line of credit, net | (18,746,439) | 1,500,000 |
| Payment of capital lease obligations | (3,422) | (5,754) |
| Restricted cash | 17,500,000 | (1,500,000) |
| Proceeds from stock offering | 2,000,000 | — |
| Proceeds from exercise of warrants, net of fees | — | 1,244,748 |
| Payment of placement agent and registration fees and other direct costs | (617,128) | (14,857) |
| Net cash provided by financing activities | 76,388 | 1,177,597 |
| Net increase (decrease) in cash and cash equivalents | 2,716,478 | (6,203,274) |
| Cash and cash equivalents | | |
| Beginning of period | 148,230 | 22,313,717 |
| End of period | \$ 2,864,708 | \$ 16,110,443 |
| Supplemental cash flows disclosures: | | |
| Cash paid during the period for interest | \$ 112,561 | \$ 12,564 |
| Supplemental disclosure of non-cash financing activity | | |
| Fair value of warrants issued in stock offering | \$ 1,676,282 | — |
| Initial fair value of preferred stock issued in offering | \$ 380,600 | — |
| Conversion of preferred stock to common stock | \$ 464,286 | — |

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

AKEENA SOLAR, INC.
Notes to Condensed Consolidated Financial Statements
March 31, 2009
(Unaudited)

1. Basis of Presentation and Description of Business

Basis of Presentation — Interim Financial Information

The accompanying condensed consolidated financial statements are unaudited and have been prepared in accordance with generally accepted accounting principles for interim financial information. They should be read in conjunction with the financial statements and related notes to the financial statements of Akeena Solar, Inc. (the “Company”) for the years ended December 31, 2008 and 2007 appearing in the Company’s Form 10-K and Form 10-KSB. The March 31, 2009 unaudited interim consolidated financial statements included in this Quarterly Report on Form 10-Q have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission (“SEC”). Certain information and note disclosures normally included in the annual financial statements filed with the Annual Report on Form 10-K have been condensed or omitted pursuant to those rules and regulations. In the opinion of management, all adjustments, consisting of normal recurring accruals, necessary for a fair statement of the results of operations for the interim periods presented have been reflected herein. The results of operations for interim periods are not necessarily indicative of the results to be expected for the entire year.

Description of Business

Akeena Solar, Inc. was incorporated in February 2001 in the State of California and elected at that time to be taxed as an S Corporation. During June 2006, the Company reincorporated in the State of Delaware and became a C Corporation. On August 11, 2006, the Company entered into a reverse merger transaction (the “Merger”) with Fairview Energy Corporation, Inc. (“Fairview”). Pursuant to the merger agreement, the stockholders of Akeena Solar received one share of Fairview common stock for each issued and outstanding share of Akeena Solar common stock. Akeena Solar’s common shares were also adjusted from \$0.01 par value to \$0.001 par value at the time of the Merger. Subsequent to the closing of the Merger, the former stockholders of Akeena Solar held a majority of Fairview’s outstanding common stock. Since the stockholders of Akeena Solar owned a majority of the outstanding shares of Fairview common stock immediately following the Merger, and the management and board of Akeena Solar became the management and board of Fairview immediately following the Merger, the Merger was accounted for as a reverse merger transaction and Akeena Solar was deemed to be the acquirer. The assets, liabilities and the historical operations prior to the Merger are those of Akeena Solar. Subsequent to the Merger, the consolidated financial statements include the assets, liabilities and the historical operations of Akeena Solar and Fairview from the closing date of the Merger.

The Company is engaged in a single business segment, the design and installation of solar power systems for residential and commercial customers.

2. Significant Accounting Policies

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Revenue Recognition

Revenue from installation of a system is recognized when (1) persuasive evidence of an arrangement exists, (2) delivery has occurred or services have been rendered, (3) the sales price is fixed or determinable, and (4) collection of

the related receivable is reasonably assured. In general, the Company recognizes revenue upon completion of a system installation for residential installations and the Company recognizes revenue under the percentage-of-completion method for commercial installations. Revenue recognition methods for revenue streams that fall under other categories are determined based on facts and circumstances.

Defective solar panels or inverters are covered under the manufacturer warranty. In the event that a panel or inverter needs to be replaced, the Company will replace the defective item within the manufacturer's warranty period (between 5-25 years). See the "Manufacturer and installation warranties" discussion below.

Deferred revenue consists of installations initiated but not completed within the reporting period.

Cash and Cash Equivalents

The Company considers all highly liquid investments with maturities of three months or less, when purchased, to be cash equivalents. The Company maintains cash and cash equivalents which consist principally of demand deposits with high credit quality financial institutions. At certain times, such amounts exceed FDIC insurance limits. The Company has not experienced any losses on these investments.

Manufacturer and Installation Warranties

The Company warrants its products for various periods against defects in material or installation workmanship. The Company provides for a 5-year or a 10-year warranty on the installation of a system and all equipment and incidental supplies other than solar panels and inverters that are covered under the manufacturer warranty. The manufacturer warranty on the solar panels and the inverters range from 5 to 25 years. The Company assists its customers in the event that the manufacturer warranty needs to be used to replace a defected panel or inverter. The Company records a provision for the installation warranty, within cost of sales, based on its historical experience and management's expectations of the probable future cost to be incurred in honoring its warranty commitment. The liability for the installation warranty of approximately \$1.1 million at March 31, 2009 and December 31, 2008, is included within "Accrued warranty" in the accompanying condensed consolidated balance sheets.

The liability for the installation warranty consists of the following:

| | March 31, 2009 (Unaudited) | December 31, 2008 |
|---|-------------------------------|----------------------|
| Beginning accrued warranty balance | \$ 1,056,655 | \$ 647,706 |
| Reduction for labor payments and claims made under the warranty | (28,760) | (397,382) |
| Accruals related to warranties issued during the period | 88,653 | 975,601 |
| Adjustments relating to changes in warranty estimates | — | (169,270) |
| Ending accrued warranty balance | \$ 1,116,548 | \$ 1,056,655 |

Recent Accounting Pronouncements

Effective January 1, 2009, the Company adopted the provisions of Emerging Issues Task Force (EITF) EITF 07-05, Determining Whether an Instrument (or Embedded Feature) Is Indexed to an Entity's Own Stock, ("EITF 07-05"). EITF 07-05 applies to any freestanding financial instruments or embedded features that have the characteristics of a derivative, as defined by SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," and to any freestanding financial instruments that are potentially settled in an entity's own common stock. As a result of adopting EITF 07-05, warrants to purchase 588,010 shares of our common stock previously treated as equity pursuant to the derivative treatment exemption were no longer afforded equity treatment. The warrants had exercise prices ranging from \$2.75-\$3.95 and expire in March and June 2010. As such, effective January 1, 2009, the Company reclassified the fair value of these warrants to purchase common stock, which had exercise price reset features, from equity to liability status as if these warrants were treated as a derivative liability since their date of issue in March and June 2007. On January 1, 2009, the Company reclassified from additional paid-in capital, as a cumulative effect adjustment, \$998,000 to beginning retained earnings and \$289,000 to common stock warrant liability to recognize the fair value of such warrants on such date. The fair value of these warrants to purchase common stock increased to \$1.6 million as of March 31, 2009. As such, we recognized a \$1.3 million non-cash charge from the change in fair value of these warrants for the three months ended March 31, 2009.

In September 2006, the Financial Accounting Standards Board (FASB) issued SFAS No. 157, Fair Value Measurements (SFAS No. 157), and in February 2008, the FASB amended SFAS No. 157 by issuing FSP FAS 157-1, Application of FASB Statement No. 157 to FASB Statement No. 13 and Other Accounting Pronouncements That Address Fair Value Measurements for Purposes of Lease Classification or Measurement under Statement 13, and FSP FAS 157-2, Effective Date of FASB Statement No. 157 (collectively SFAS No. 157). SFAS No. 157 defines fair

value, establishes a framework for measuring fair value and expands disclosure of fair value measurements. SFAS No. 157 is applicable to other accounting pronouncements that require or permit fair value measurements, except those relating to lease accounting, and accordingly does not require any new fair value measurements. SFAS No. 157 was effective for financial assets and liabilities in fiscal years beginning after November 15, 2007, and for non-financial assets and liabilities in fiscal years beginning after November 15, 2008 except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis. Our adoption of the provisions of SFAS No. 157 on January 1, 2008, with respect to financial assets and liabilities measured at fair value, did not have an effect on our financial statements for the year ended December 31, 2008. In October 2008, the FASB issued FSP FAS 157-3, Determining the Fair Value of a Financial Asset When the Market for That Asset is Not Active (FSP FAS 157-3). FSP FAS 157-3 clarifies the application of SFAS No. 157 in a market that is not active and provides an example to illustrate key considerations in determining the fair value of a financial asset when the market for that financial asset is not active. FSP FAS 157-3 became effective immediately upon issuance, and its adoption did not have an effect on our financial statements. We currently determine the fair value of our property and equipment when assessing long-lived asset impairments and SFAS No. 157 was effective for these fair value assessments as of January 1, 2009. In April 2009, the FASB issued SFAS No. 157-4, Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly (SFAS 157-4). SFAS 157-4 provides additional guidance for estimating fair value in accordance with SFAS Statement No. 157, Fair Value Measurements, when the volume and level of activity for the asset or liability have significantly decreased. SFAS 157-4 also includes guidance on identifying circumstances that indicate a transaction is not orderly. SFAS 157-4 emphasizes that even if there has been a significant decrease in the volume and level of activity for the asset or liability and regardless of the valuation technique(s) used, the objective of a fair value measurement remains the same. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. SFAS 157-4 is effective for interim and annual reporting periods ending after June 15, 2009, and is applied prospectively. We do not believe the adoption of this standard will have a material impact on our consolidated financial position, results of operations and cash flows.

The fair value hierarchy distinguishes between assumptions based on market data (observable inputs) and an entity's own assumptions (unobservable inputs). The hierarchy consists of three levels:

- Level one — Quoted market prices in active markets for identical assets or liabilities;
- Level two — Inputs other than level one inputs that are either directly or indirectly observable; and
- Level three — Unobservable inputs developed using estimates and assumptions, which are developed by the reporting entity and reflect those assumptions that a market participant would use.

Determining which category an asset or liability falls within the hierarchy requires significant judgment. We evaluate our hierarchy disclosures each quarter. Assets and liabilities measured at fair value on a recurring basis are summarized as follows (unaudited):

| Assets | Level 1 | Level 2 | Level 3 | March 31, 2009 |
|--------------------------------|--------------|---------|---------|----------------|
| Fair value of cash equivalents | 1,001,731 | — | — | 1,001,731 |
| Total | \$ 1,001,731 | \$ — | \$ — | 1,001,731 |

| Liabilities | Level 1 | Level 2 | Level 3 | March 31, 2009 |
|---|---------|--------------|------------|----------------|
| Fair value of common stock warrants | \$ — | \$ 3,043,112 | \$ — | \$ 3,043,112 |
| Accrued rent related to office closures | — | — | 242,143 | 242,143 |
| Total | \$ — | \$ 3,043,112 | \$ 242,143 | \$ 3,285,255 |

Cash equivalents represent the fair value of the Company's investment in a money market account as of March 31, 2009. A discussion of the valuation techniques used to measure fair value for the common stock warrants is in Note 11. The accrued rent relates to non-cash charges for the closures of our Bakersfield and Manteca, California, Milford, Connecticut, and Denver, Colorado locations, calculated by discounting the future lease payments to their present value using a risk-free discount rate of 1.2%.

The following table shows the changes in Level 3 liabilities measured at fair value on a recurring basis for the quarter ended March 31, 2009:

| | Other Liabilities* |
|--|--------------------|
| Beginning balance | \$ 200,784 |
| Total realized and unrealized gains or losses | 517 |
| Purchases, sales, repayments, settlements and issuances, net | 40,842 |
| Net transfers in and/or (out) of level 3 | — |
| Ending balance | \$ 242,143 |

* Represents the estimated fair value of the office closures included in accrued and other long-term liabilities.

In December 2007, the FASB issued SFAS No. 160, Noncontrolling Interests in Consolidated Financial Statements, an amendment of Accounting Research Bulletin ARB No. 51, Consolidated Financial Statements (SFAS No. 160). SFAS No. 160 requires (i) that non-controlling (minority) interests be reported as a component of stockholders' equity, (ii) that net income attributable to the parent and to the non-controlling interest be separately identified in the consolidated statement of operations, (iii) that changes in a parent's ownership interest while the parent retains its controlling interest be accounted for as equity transactions, (iv) that any retained non-controlling equity investment upon the deconsolidation of a subsidiary be initially measured at fair value and, (v) that sufficient disclosures are provided that clearly identify and distinguish between the interests of the parent and the interests of the non-controlling owners. SFAS No. 160 is effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years. We adopted SFAS No. 160 for our fiscal year beginning January 1, 2009, and the adoption did not have any impact on our consolidated financial position, results of operations and cash flows.

In December 2007, the FASB issued SFAS No. 141(R), Business Combinations (SFAS No. 141(R)). SFAS No. 141(R) will significantly change the accounting for business combinations. Under SFAS 141(R), an acquiring entity will be required to recognize all the assets acquired and liabilities assumed in a transaction at the acquisition-date fair value with limited exceptions. SFAS No. 141(R) will change the accounting treatment for certain specific acquisition related items including: (i) expensing acquisition related costs as incurred; (ii) valuing noncontrolling interests at fair value at the acquisition date of a controlling interest; and (iii) expensing restructuring costs associated with an acquired business. SFAS No. 141(R) also includes a substantial number of new disclosure requirements. SFAS No. 141(R) is applied prospectively to business combinations for which the acquisition date is on or after January 1, 2009. SFAS No. 141(R) will have an impact on our accounting for any future business combinations.

In March 2008, the FASB issued SFAS No. 161, Disclosures about Derivative Instruments and Hedging Activities — an amendment of FASB Statement No. 133 (SFAS No. 161). SFAS No. 161 requires qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about fair value amounts and gains and losses on derivative instruments, and disclosures about credit-risk-related contingent features in derivative agreements. SFAS No. 161 was effective for fiscal years beginning after November 15, 2008. As of March 31, 2009, we have derivatives of \$3,043,112 related to the common stock warrant liabilities. The derivatives instruments were not entered into as hedging activities, and the change in value of the liability is recorded as a component of other income (expense) as "Adjustment to the fair value of common stock warrants."

In April 2008, the FASB issued FASB Staff Position (FSP) No. FAS 142-3, Determination of the Useful Life of Intangible Assets (FSP FAS 142-3). FSP FAS 142-3 amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under SFAS No. 142, Goodwill and Other Intangible Asset (SFAS 142). More specifically, FSP FAS 142-3 removes the requirement under paragraph 11 of SFAS 142 to consider whether an intangible asset can be renewed without substantial cost or material modifications to the existing terms and conditions and instead, requires an entity to consider its own historical experience in renewing similar arrangements. FSP FAS 142-3 also requires expanded disclosure related to the determination of intangible asset useful lives. The adoption of this FSP on January 1, 2009 may impact any intangible assets we acquire in future transactions.

In November 2008, the Emerging Issues Task Force (EITF) reached consensus on EITF Issue No. 08-7, Accounting for Defensive Intangible Assets (EITF 08-7). A defensive asset is an acquired intangible asset where the acquirer has no intention of using, or intends to discontinue use of, the intangible asset but holds it to prevent competitors from obtaining any benefit from it. The acquired defensive asset will be treated as a separate unit of accounting and the useful life assigned will be based on the period during which the asset would diminish in value. The adoption of this EITF on January 1, 2009 may impact any intangible assets we acquire in future transactions.

In April 2009, the FASB issued Staff Position No. FAS 107-1 and APB 28-1, Interim Disclosures about Fair Value of Financial Instruments (FSP FAS 107-1 and APB 28-1). FSP FAS 107-1 and APB 28-1 extends the disclosure requirements of SFAS 107 to interim period financial statements, in addition to the existing requirements for annual periods and reiterates SFAS 107's requirement to disclose the methods and significant assumptions used to estimate fair value. FSP FAS 107-1 and APB 28-1 is effective for our interim and annual periods commencing with our June 30, 2009 consolidated financial statements and will be applied on a prospective basis. We believe the adoption of FSP FAS 107-1 and APB 28-1 will not have a material impact on consolidated financial position, results of operations and cash flows.

In April 2009, the FASB issued SFAS 107-1 and APB 28-1, Interim Disclosures about Fair Value of Financial Instruments (SFAS 107-1). SFAS 107-1 amends FASB No. 107, Disclosures about Fair Value of Financial Instruments, to require disclosures about fair value of financial instruments for interim reporting periods of publicly traded companies as well as in annual financial statements. SFAS also amends APB Opinion No. 28, Interim Financial Reporting, to require those disclosures in summarized financial information at interim reporting periods. SFAS 107-1 is effective for interim and annual reporting periods ending after June 15, 2009. We do not believe the adoption of this standard will have a material impact on our consolidated financial position, results of operations and cash flows.

3. Accounts Receivable and Notes Receivable

Accounts receivable consists of the following:

| | March 31, 2009 (Unaudited) | December 31, 2008 |
|---------------------------------------|-------------------------------|----------------------|
| State rebates receivable | \$ 3,931,521 | \$ 4,894,943 |
| Trade accounts | 1,774,630 | 3,909,690 |
| Rebate receivable assigned to vendor | — | 2,144 |
| Less: Allowance for doubtful accounts | (316,047) | (1,146,738) |
| | \$ 5,390,104 | \$ 7,660,039 |

4. Inventory

Inventory consists of the following:

| | March 31, 2009 (Unaudited) | December 31, 2008 |
|--|-------------------------------|----------------------|
| Work in process | \$ 1,422,335 | \$ 1,554,604 |
| Finished goods | 5,722,669 | 8,992,781 |
| Less: provision for obsolete inventory | (51,813) | |