

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 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 December 31, 2015

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: 001-33301

**ACCURAY INCORPORATED**

(Exact Name of Registrant as Specified in Its Charter)

**Delaware**

(State or Other Jurisdiction of Incorporation or Organization)

**20-8370041**

(IRS Employer Identification Number)

**1310 Chesapeake Terrace**

**Sunnyvale, California 94089**

(Address of Principal Executive Offices Including Zip Code)

**(408) 716-4600**

(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 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 (§ 229.405 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 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

Smaller reporting company

(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  No

As of January 25, 2016, there were 80,842,841 shares of the Registrant's Common Stock, par value \$0.001 per share, outstanding.

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**PART I. FINANCIAL INFORMATION**

**Item 1. Condensed Consolidated Financial Statements**

**Accuray Incorporated**  
**Condensed Consolidated Balance Sheets**  
(in thousands, except share amounts and par value)  
(Unaudited)

|  | December 31,<br>2015 | June 30,<br>2015 (1) |
|--|----------------------|----------------------|
| <b>Assets</b>  |                      |                      |
| Current assets:  |                      |                      |
| Cash and cash equivalents  | \$ 88,451            | \$ 79,551            |
| Short-term investments   | 67,304               | 64,306               |
| Restricted cash  | 2,596                | 3,734                |
| Accounts receivable, net of allowance for doubtful accounts of \$837 and \$709 as of December 31, 2015 and June 30, 2015, respectively | 66,044               | 77,727               |
| Inventories  | 111,513              | 106,151              |
| Prepaid expenses and other current assets  | 13,598               | 15,991               |
| Deferred cost of revenue   | 8,834                | 6,869                |
| Total current assets   | 358,340              | 354,329              |
| Property and equipment, net  | 29,550               | 31,829               |
| Goodwill   | 57,892               | 58,054               |
| Intangible assets, net   | 11,587               | 15,564               |
| Deferred cost of revenue   | 2,152                | 1,500                |
| Other assets   | 13,804               | 8,695                |
| Total assets   | \$ 473,325           | \$ 469,971           |
| <b>Liabilities and stockholders' equity</b>  |                      |                      |
| Current liabilities:   |                      |                      |
| Accounts payable   | \$ 19,561            | \$ 13,096            |
| Accrued compensation   | 20,484               | 21,934               |
| Other accrued liabilities  | 23,839               | 18,720               |
| Short-term debt  | 96,551               | —                    |
| Customer advances  | 19,377               | 19,385               |
| Deferred revenue   | 94,386               | 96,780               |
| Total current liabilities  | 274,198              | 169,915              |

|   |            |            |
|---|------------|------------|
| Long-term liabilities:  |            |            |
| Long-term other liabilities   | 10,829     | 10,934     |
| Deferred revenue  | 17,257     | 10,489     |
| Long-term debt  | 110,172    | 202,853    |
| Total liabilities   | 412,456    | 394,191    |
| Commitment and contingencies (Note 5)   |            |            |
| Stockholders' Equity:   |            |            |
| Preferred stock, \$0.001 par value; authorized: 5,000,000 shares; no shares issued and outstanding  | —          | —          |
| Common stock, \$0.001 par value; authorized: 200,000,000 shares as of December 31, 2015 and June 30, 2015 respectively; issued and outstanding: 80,835,472 and 79,477,838 shares at December 31, 2015 and June 30, 2015, respectively | 81         | 79         |
| Additional paid-in capital  | 476,387    | 471,430    |
| Accumulated other comprehensive loss  | (1,243)    | (426)      |
| Accumulated deficit   | (414,356)  | (395,303)  |
| Total stockholders' equity  | 60,869     | 75,780     |
| Total liabilities and stockholders' equity  | \$ 473,325 | \$ 469,971 |

(1) The condensed consolidated balance sheet at June 30, 2015 has been derived from audited consolidated financial statements.

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

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**Accuray Incorporated**  
**Condensed Consolidated Statements of Operations and Comprehensive Loss**  
(in thousands, except per share amounts)  
(Unaudited)

|   | Three Months Ended December |             | Six Months Ended December |             |
|---|-----------------------------|-------------|---------------------------|-------------|
|   | 2015                        | 2014        | 2015                      | 2014        |
| Net revenue:  |                             |             |                           |             |
| Products  | \$ 55,759                   | \$ 47,650   | \$ 95,754                 | \$ 80,665   |
| Services  | 53,153                      | 50,505      | 102,789                   | 99,871      |
| Total net revenue   | 108,912                     | 98,155      | 198,543                   | 180,536     |
| Cost of revenue:  |                             |             |                           |             |
| Cost of products  | 32,717                      | 27,171      | 55,734                    | 47,836      |
| Cost of services  | 33,624                      | 32,495      | 66,340                    | 66,410      |
| Total cost of revenue   | 66,341                      | 59,666      | 122,074                   | 114,246     |
| Gross profit  | 42,571                      | 38,489      | 76,469                    | 66,290      |
| Operating expenses:   |                             |             |                           |             |
| Research and development  | 14,931                      | 13,917      | 29,227                    | 28,066      |
| Selling and marketing   | 15,076                      | 15,802      | 28,493                    | 33,776      |
| General and administrative                                      | 12,688                      | 12,361      | 26,104                    | 23,311      |
| Total operating expenses  | 42,695                      | 42,080      | 83,824                    | 85,153      |
| Loss from operations  | (124)                       | (3,591)     | (7,355)                   | (18,863)    |
| Other expense, net  | (5,070)                     | (5,528)     | (10,161)                  | (10,989)    |
| Loss before provision for income taxes                          | (5,194)                     | (9,119)     | (17,516)                  | (29,852)    |
| Provision for income taxes                                      | 833                         | 873         | 1,537                     | 1,790       |
| Net loss  | \$ (6,027)                  | \$ (9,992)  | \$ (19,053)               | \$ (31,642) |
| Net loss per share — basic and diluted                          | \$ (0.08)                   | \$ (0.13)   | \$ (0.24)                 | \$ (0.41)   |
| Weighted average common shares used in computing loss per share |                             |             |                           |             |
| Basic and diluted   | 80,346                      | 77,924      | 80,053                    | 77,607      |
| Net loss  | \$ (6,027)                  | \$ (9,992)  | \$ (19,053)               | \$ (31,642) |
| Foreign currency translation adjustment                         | (469)                       | (624)       | (727)                     | (1,066)     |
| Unrealized gain (loss) on investments, net of tax               | (128)                       | 2           | (90)                      | (139)       |
| Comprehensive loss  | \$ (6,624)                  | \$ (10,614) | \$ (19,870)               | \$ (32,847) |

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

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**Condensed Consolidated Statements of Cash Flows**  
(in thousands)  
(Unaudited)

|   | Six Months Ended<br>December 31, |             |
|---|----------------------------------|-------------|
|   | 2015                             | 2014        |
| <b>Cash Flows From Operating Activities</b>   |                                  |             |
| Net loss  | \$ (19,053)                      | \$ (31,642) |
| Adjustments to reconcile net loss to net cash provided by (used in) operating activities: |                                  |             |
| Depreciation and amortization   | 9,061                            | 9,960       |
| Share-based compensation  | 5,879                            | 7,127       |
| Amortization of debt issuance costs   | 771                              | 732         |
| Amortization and accretion of discount and premium on investments                         | 536                              | 488         |
| Accretion of interest on debt   | 3,870                            | 3,540       |
| Recovery of (provision for) bad debt, net   | 128                              | (51)        |
| Provision for write-down of inventories   | 729                              | 747         |
| Loss on disposal of property and equipment  | 8                                | —           |
| Changes in assets and liabilities:  |                                  |             |
| Restricted cash   | 950                              | —           |
| Accounts receivable   | 10,959                           | 6,619       |
| Inventories   | (5,669)                          | (18,628)    |
| Prepaid expenses and other assets   | (3,546)                          | 2,750       |
| Deferred cost of revenue  | (2,678)                          | 1,933       |
| Accounts payable  | 6,715                            | 1,313       |
| Accrued liabilities   | 5,414                            | (3,050)     |
| Customer advances   | 294                              | 732         |
| Deferred revenue  | 5,912                            | 4,445       |
| Net cash provided by (used in) operating activities                                       | 20,280                           | (12,985)    |
| <b>Cash Flows From Investing Activities</b>   |                                  |             |
| Purchases of property and equipment, net  | (4,125)                          | (4,170)     |
| Purchases of investments  | (33,130)                         | (56,011)    |
| Sales and maturities of investments   | 29,505                           | 81,420      |
| Net cash (used in) provided by investing activities                                       | (7,750)                          | 21,239      |
| <b>Cash Flows From Financing Activities</b>   |                                  |             |
| Proceeds from employee stock plans  | 2,055                            | 3,034       |
| Taxes paid related to net share settlement of equity awards                               | (2,841)                          | (394)       |
| Net cash (used in) provided by financing activities                                       | (786)                            | 2,640       |
| Effect of exchange rate changes on cash and cash equivalents                              | (2,844)                          | (5,967)     |
| Net increase in cash and cash equivalents   | 8,900                            | 4,927       |
| Cash and cash equivalents at beginning of period  | 79,551                           | 92,346      |
| Cash and cash equivalents at end of period  | \$ 88,451                        | \$ 97,273   |

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

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**Accuray Incorporated**  
**Notes to Condensed Consolidated Financial Statements**  
(Unaudited)

**1. Summary of Significant Accounting Policies**

**Description of Business**

Accuray Incorporated (together with its subsidiaries, the “Company” or “Accuray”) is incorporated in Delaware and has its principal place of business in Sunnyvale, California. The Company designs, develops and sells advanced radiosurgery and radiation therapy systems for the treatment of tumors throughout the body. The Company has offices in the United States, Switzerland, China and Japan and conducts its business worldwide.

**Basis of Presentation and Principles of Consolidation**

The condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All significant inter-company transactions and balances have been eliminated in consolidation.

The accompanying condensed consolidated financial statements have been prepared in accordance with United States generally accepted accounting principles (“GAAP”), pursuant to the rules and regulations of the Securities and Exchange Commission (the “SEC”). Certain information and note disclosures have been condensed or omitted pursuant to such rules and regulations. The unaudited condensed consolidated financial statements have been prepared on the same basis as the annual financial statements and, in the opinion of management, reflect all adjustments, which include only normal recurring adjustments, necessary for a fair presentation of the periods presented. The results for the three and six months ended December 31, 2015 are not necessarily indicative of the results to be expected for the year ending June 30, 2016, for any other future interim period or future year.

These condensed consolidated financial statements should be read in conjunction with the Company’s audited consolidated financial statements and accompanying notes for the year ended June 30, 2015 included in the Company’s Annual Report on Form 10-K filed with the SEC on August 28, 2015. The

Company's significant accounting policies are described in Note 2 to those audited consolidated financial statements and there have been no material changes to such policies.

### **Recent Accounting Standard Update Not Yet Effective**

In May 2014, the FASB issued Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers: Topic 606* (ASU 2014-09), to supersede nearly all existing revenue recognition guidance under GAAP. The core principle of ASU 2014-09 is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration that is expected to be received for those goods or services. ASU 2014-09 defines a five step process to achieve this core principle and, in doing so, it is possible more judgment and estimates may be required within the revenue recognition process than required under existing GAAP including identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each separate performance obligation. On July 9, 2015, FASB approved a one-year deferral of the effective period for ASU 2014-09. The standard will be effective for the Company for the first quarter of fiscal 2019, but entities will be permitted to early adopt the standard as of the original effective date, which would be the first quarter of fiscal 2018 for the Company. The Company may adopt either of two methods: (i) retrospective to each prior reporting period presented with the option to elect certain practical expedients as defined within ASU 2014-09; or (ii) retrospective with the cumulative effect of initially applying ASU 2014-09 recognized at the date of initial application and providing certain additional disclosures as defined per ASU 2014-09. The Company has not yet selected a transition method, has not yet determined whether it will select early adoption and is currently evaluating the impact of pending adoption of ASU 2014-09 on its consolidated financial statements and related disclosures.

### **Use of Estimates**

The preparation of condensed consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosures at the date of the financial statements. Key estimates and assumptions made by the Company relate to revenue recognition, assessment of recoverability of goodwill and intangible assets, valuation of inventories, share-based compensation expense, income taxes, allowance for doubtful accounts, loss contingencies and corporate bonus expenses. Actual results could differ materially from those estimates.

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### **Concentration of Credit and Other Risks**

The Company's cash, cash equivalents and investments are deposited with several major financial institutions. At times, deposits in these institutions exceed the amount of insurance provided on such deposits. The Company has not experienced any losses in such accounts and does not believe that it is exposed to any significant risk of loss on these balances.

For the three months ended December 31, 2015 and 2014, there were no customers that represented 10% or more of total net revenue. For the six months ended December 31, 2015, there was one customer that represented 11% of total net revenue. For the six months ended December 31, 2014, there were no customers that represented 10% or more of total net revenue. No customer accounted for more than 10% of the Company's total accounts receivable as of December 31, 2015. One customer accounted for 18% of the Company's total accounts receivable as of June 30, 2015.

Accounts receivable are typically not collateralized. The Company performs ongoing credit evaluations of its customers and maintains reserves for potential credit losses. Accounts receivable are deemed past due in accordance with the contractual terms of the agreement. Accounts are charged against the allowance for doubtful accounts once collection efforts are unsuccessful.

Single source suppliers presently provide the Company with several components. In most cases, if a supplier was unable to deliver these components, the Company believes that it would be able to find other sources for these components subject to any regulatory qualifications, if required.

### **Revenue Recognition**

The Company earns revenue from the sale of products and related services. The Company records its revenues net of any value added or sales tax. For arrangements with multiple elements, the Company allocates arrangement fees to products and services based upon Vendor Specific Objective Evidence ("VSOE") of fair value of the respective elements, Third-Party Evidence ("TPE"), or Best Estimate of Selling Price ("BESP"), using the relative selling price method.

#### *Product and Service Revenue*

The majority of product revenue is generated from sales of CyberKnife and TomoTherapy systems. If the Company is responsible for installation, the Company recognizes revenue after installation and acceptance of the system. Otherwise, revenue is recognized upon delivery, assuming all other revenue recognition criteria are met.

The Company offers its systems with post-contract customer support ("PCS") contracts, installation services, training and professional services. PCS contracts provide planned and corrective maintenance services, software updates, bug fixes, as well as call-center support. Service revenue is generated primarily from PCS (warranty period services and post warranty services), installation services, training, parts and upgrades that are sold under service contracts and professional services. PCS revenue is deferred and recognized over the service period. Installation service revenue is recognized concurrent with system revenue. Training and professional service revenues that are not deemed essential to the functionality of the systems are recognized as such services are performed.

Costs associated with service revenue are expensed when incurred, except when those costs are related to parts or system upgrades where revenue recognition has been deferred. In those cases, the costs are deferred and are recognized over the period of revenue recognition.

### **Net Loss Per Common Share**

Basic and diluted net loss per share is computed by dividing net loss attributable to stockholders by the weighted average number of common shares outstanding during the period.

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A reconciliation of the numerator and denominator used in the calculation of basic and diluted net loss per share follows (in thousands):

|  | Three Months Ended<br>December 31, |            | Six Months Ended<br>December 31, |             |
|--|------------------------------------|------------|----------------------------------|-------------|
|  | 2015                               | 2014       | 2015                             | 2014        |
| <b>Numerator:</b>  |                                    |            |                                  |             |
| Net loss used in computing net loss per share                              | \$ (6,027)                         | \$ (9,992) | \$ (19,053)                      | \$ (31,642) |
| <b>Denominator:</b>  |                                    |            |                                  |             |
| Weighted average shares used in computing basic and diluted loss per share | 80,346                             | 77,924     | 80,053                           | 77,607      |

The potentially dilutive shares of the Company's common stock resulting from the assumed exercise of outstanding stock options, the vesting of Restricted Stock Units (RSU), Market Stock Units (MSU) and Performance Stock Units (PSU), and the purchase of shares under the Employee Stock Purchase Program (ESPP), as determined under the treasury stock method, are excluded from the computation of diluted net loss per share because their effect would have been anti-dilutive. Additionally, the 3.75% Convertible Senior Notes due August 1, 2016 (the "3.75% Convertible Notes"), the 3.50% Convertible Senior Notes due February 1, 2018 (the "3.50% Convertible Notes") and the 3.50% Series A Convertible Notes (the "3.50% Series A Convertible Notes") due February 1, 2018 (together, the "Convertible Notes") are included in the calculation of diluted net income per share only if their inclusion is dilutive. For the three months ended December 31, 2015 and 2014, respectively, the potentially dilutive shares under the Convertible Notes were excluded from the calculation of diluted net loss per share as their inclusion would have been anti-dilutive. The following table sets forth all potentially dilutive securities excluded from the computation in the table above because their effect would have been anti-dilutive (in thousands):

|                                  | As of December 31, |        |
|----------------------------------|--------------------|--------|
|                                  | 2015               | 2014   |
| Stock options                    | 2,409              | 2,861  |
| RSUs, PSUs and MSUs              | 4,834              | 5,069  |
| 3.50% Convertible Notes          | 8,378              | 8,378  |
| 3.50% Series A Convertible Notes | 2,781              | 3,886  |
|                                  | 18,402             | 20,194 |

**Outstanding Convertible Notes—Diluted Share Impact**

The 3.75% Convertible Notes and 3.50% Series A Convertible Notes have an optional physical (share), cash or combination settlement feature and contain certain conditional conversion features. Due to the optional cash settlement feature and management's intent to settle the principal amount thereof in cash, the conversion shares underlying the outstanding principal amount of the 3.75% Convertible Notes and the 3.50% Series A Convertible Notes, totaling approximately 10.6 million shares and 13.2 million shares, respectively, were not included in the potentially diluted share count table above. The Company's average stock price did not exceed the conversion price of the 3.75% Convertible Notes as of December 31, 2015 and 2014, respectively. The 2.8 and 3.9 million potentially dilutive shares of the 3.50% Series A Convertible Notes as of December 31, 2015 and 2014, respectively, included in the table above represent the premium over the principal amount due to the higher average share price above the conversion price. The number of premium shares included in the Company's diluted share count will vary with fluctuations in the Company's share price. Higher actual share prices result in a greater number of premium shares.

**Segment Information**

The Company has determined that it operates in only one segment, as it only reports profit and loss information on an aggregate basis to its chief operating decision maker. Revenue by geographic region is based on the shipping addresses of the Company's customers. The following summarizes revenue by geographic region (in thousands):

|  | Three Months Ended<br>December 31, |           | Six Months Ended<br>December 31, |            |
|--|------------------------------------|-----------|----------------------------------|------------|
|  | 2015                               | 2014      | 2015                             | 2014       |
| Americas                                 | \$ 51,000                          | \$ 45,717 | \$ 96,290                        | \$ 84,195  |
| Europe, Middle East, India and Africa    | 15,739                             | 26,094    | 38,773                           | 57,031     |
| Asia-Pacific (excluding Japan and India) | 35,784                             | 14,470    | 52,766                           | 19,352     |
| Japan                                    | 6,389                              | 11,874    | 10,714                           | 19,958     |
| Total                                    | \$ 108,912                         | \$ 98,155 | \$ 198,543                       | \$ 180,536 |

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Information regarding geographic areas in which the Company has long lived tangible assets is as follows (in thousands):

|  | December 31,<br>2015 | June 30,<br>2015 |
|--|----------------------|------------------|
| Americas                                 | \$ 25,797            | \$ 28,182        |
| Europe, Middle East, India and Africa    | 686                  | 929              |
| Asia-Pacific (excluding Japan and India) | 1,030                | 455              |
| Japan                                    | 2,037                | 2,263            |
| Total                                    | \$ 29,550            | \$ 31,829        |

## 2. Balance Sheet Components

### Financing receivables

A financing receivable is a contractual right to receive money, on demand or on fixed or determinable dates, that is recognized as an asset in the Company's balance sheet. The Company's financing receivables, consisting of its accounts receivable with contractual maturities of more than one year, totaled \$8.1 million and \$1.6 million at December 31, 2015 and June 30, 2015, respectively, and are included in Other Assets in the consolidated balance sheets. There was no balance in the allowance for doubtful accounts related to such financing receivables as of December 31, 2015 and June 30, 2015, respectively, as revenue is recognized on a cash basis for these receivables.

### Inventories

Inventories consisted of the following (in thousands):

|                 | December 31,<br>2015 | June 30,<br>2015  |
|-----------------|----------------------|-------------------|
| Raw materials   | \$ 49,391            | \$ 46,356         |
| Work-in-process | 18,352               | 15,445            |
| Finished goods  | 43,770               | 44,350            |
| Inventories     | <u>\$ 111,513</u>    | <u>\$ 106,151</u> |

### Property and equipment, net

Property and equipment, net consisted of the following (in thousands):

|                                | December 31,<br>2015 | June 30,<br>2015 |
|--------------------------------|----------------------|------------------|
| Furniture and fixtures         | \$ 4,662             | \$ 4,674         |
| Computer and office equipment  | 12,440               | 11,808           |
| Software                       | 11,094               | 10,992           |
| Leasehold improvements         | 20,952               | 19,428           |
| Machinery and equipment        | 49,548               | 47,031           |
| Construction in progress       | 5,355                | 8,273            |
|                                | <u>104,051</u>       | <u>102,206</u>   |
| Less: Accumulated depreciation | (74,501)             | (70,377)         |
| Property and equipment, net    | <u>\$ 29,550</u>     | <u>\$ 31,829</u> |

Depreciation expense related to property and equipment for the three and six months ended December 31, 2015 was \$2.5 million and \$5.1 million, respectively. Depreciation expense related to property and equipment for the three and six months ended December 31, 2014 was \$3.0 million and \$6.0 million, respectively.

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## 3. Goodwill and Intangible Assets

### Goodwill

Activity related to goodwill consisted of the following (in thousands):

|  | Six Months<br>Ended<br>December 31,<br>2015 | Year<br>Ended<br>June 30,<br>2015 |
|--|---|-----------------------------------|
| Balance at the beginning of the period | \$ 58,054                                   | \$ 58,091                         |
| Currency translation                   | (162)                                       | (37)                              |
| Balance at the end of the period       | <u>\$ 57,892</u>                            | <u>\$ 58,054</u>                  |

In the second quarter of fiscal 2016, the Company performed its annual goodwill impairment test. Based on this analysis, the Company determined that there was no impairment to goodwill. The Company will continue to monitor its recorded goodwill for indicators of impairment.

### Intangible Assets

The Company's unamortized intangible assets associated with completed acquisitions at December 31, 2015 and June 30, 2015 are as follows (in thousands):

|                      | Useful Lives<br>(in years) | December 31, 2015           |                             |               | June 30, 2015               |                             |               |
|----------------------|----------------------------|-----------------------------|-----------------------------|---------------|-----------------------------|-----------------------------|---------------|
|                      |                            | Gross<br>Carrying<br>Amount | Accumulated<br>Amortization | Net<br>Amount | Gross<br>Carrying<br>Amount | Accumulated<br>Amortization | Net<br>Amount |
| Developed technology | 5 — 6                      | \$ 46,746                   | \$ (35,159)                 | \$ 11,587     | \$ 46,700                   | \$ (31,136)                 | \$ 15,564     |

The Company did not identify any triggering events that would indicate potential impairment of its definite-lived intangible and long-lived assets as of December 31, 2015 and June 30, 2015.

Amortization expense related to intangible assets for the three and six months ended December 31, 2015 was \$2.0 million and \$4.0 million, respectively. Amortization expense related to intangible assets for the three and six months ended December 31, 2014 was \$2.0 million and \$4.0 million, respectively.

The estimated future amortization expense of purchased intangible assets as of December 31, 2015 is as follows (in thousands):

| Year Ending June 30,      | Amount           |
|---------------------------|------------------|
| 2016 (remaining 6 months) | \$ 3,976         |
| 2017                      | 7,568            |
| 2018                      | 43               |
|                           | <u>\$ 11,587</u> |

#### 4. Financial Instruments

The Company considers all highly liquid investments held at major banks, certificates of deposit and other securities with original maturities of three months or less to be cash equivalents.

The Company classifies all of its investments as available-for-sale at the time of purchase because it is management's intent that these investments are available for current operations and includes these investments on its balance sheet as short-term investments. Investments with original maturities longer than three months include commercial paper, U.S. agency securities, non-U.S. government securities and investment-grade corporate debt securities. Investments classified as available-for-sale are recorded at fair market value with the related unrealized gains and losses included in accumulated other comprehensive income (loss), a

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component of stockholders' equity. Realized gains and losses are recorded based on specific identification of each security's cost basis.

The Company defines fair value as the price that would be received to sell an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The fair value hierarchy contains three levels of inputs that may be used to measure fair value, as follows:

*Level 1*— Unadjusted quoted prices that are available in active markets for the identical assets or liabilities at the measurement date.

*Level 2*— Other observable inputs available at the measurement date, other than quoted prices included in Level 1, either directly or indirectly, including:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets in non-active markets;
- Inputs other than quoted prices that are observable for the asset or liability; and
- Inputs that are derived principally from or corroborated by other observable market data.

*Level 3*— Unobservable inputs that cannot be corroborated by observable market data and require the use of significant management judgment. These values are generally determined using pricing models for which the assumptions utilize management's estimates of market participant assumptions.

The following tables summarize the amortized cost, gross unrealized gains, gross unrealized losses and fair value by significant investment category for cash, cash equivalents and short-term investments (in thousands):

|                        | December 31, 2015 |                        |                         |                           |                        |
|------------------------|-------------------|------------------------|-------------------------|---------------------------|------------------------|
|                        | Amortized Cost    | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Market Value    |                        |
|                        |                   |                        |                         | Cash and Cash Equivalents | Short-term Investments |
| Cash                   | \$ 85,262         | \$ —                   | \$ —                    | \$ 85,262                 | \$ —                   |
| Level 1                |                   |                        |                         |                           |                        |
| Money market funds     | 1,190             | —                      | —                       | 1,190                     | —                      |
|                        | 1,190             | —                      | —                       | 1,190                     | —                      |
| Level 2                |                   |                        |                         |                           |                        |
| Commercial paper       | 10,109            | —                      | —                       | 1,999                     | 8,110                  |
| U.S. agency securities | 27,000            | —                      | (103)                   | —                         | 26,897                 |
| U.S. treasury bills    | 3,991             | —                      | (6)                     | —                         | 3,985                  |
| Corporate notes        | 28,371            | —                      | (59)                    | —                         | 28,312                 |
|                        | 69,471            | —                      | (168)                   | 1,999                     | 67,304                 |
| <b>Total</b>           | <u>\$ 155,923</u> | <u>\$ —</u>            | <u>\$ (168)</u>         | <u>\$ 88,451</u>          | <u>\$ 67,304</u>       |

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|  | June 30, 2015  |                        |                         |                           |                        |
|--|----------------|------------------------|-------------------------|---------------------------|------------------------|
|  | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Market Value    |                        |
|  |                |                        |                         | Cash and Cash Equivalents | Short-term Investments |

|                                |                   |             |                |                  |                  |
|--------------------------------|-------------------|-------------|----------------|------------------|------------------|
| Cash                           | \$ 73,444         | \$ —        | \$ —           | \$ 73,444        | \$ —             |
| Level 1                        |                   |             |                |                  |                  |
| Money market funds             | 6,107             | —           | —              | 6,107            | —                |
|                                | <u>6,107</u>      | <u>—</u>    | <u>—</u>       | <u>6,107</u>     | <u>—</u>         |
| Level 2                        |                   |             |                |                  |                  |
| Commercial paper               | 11,989            | —           | —              | —                | 11,989           |
| U.S. Agency securities         | 21,999            | 6           | (14)           | —                | 21,991           |
| Non-U.S. government securities | 1,504             | —           | (3)            | —                | 1,501            |
| Corporate notes                | 28,891            | —           | (66)           | —                | 28,825           |
|                                | <u>64,383</u>     | <u>6</u>    | <u>(83)</u>    | <u>—</u>         | <u>64,306</u>    |
| <b>Total</b>                   | <b>\$ 143,934</b> | <b>\$ 6</b> | <b>\$ (83)</b> | <b>\$ 79,551</b> | <b>\$ 64,306</b> |

The Company's Level 2 investments in the table above are classified as Level 2 items because quoted prices in an active market are not readily accessible for those specific financial assets, or the Company may have relied on alternative pricing methods that do not rely exclusively on quoted prices to determine the fair value of the investments.

The Company had investments that were in an unrealized loss position as of December 31, 2015. The Company determined that (i) it does not have the intent to sell any of these investments and (ii) it is not likely that it will be required to sell any of these investments before recovery of the entire amortized cost basis. The Company reviews its investments quarterly to identify and evaluate investments that have an indication of possible impairment. As of December 31, 2015, the Company anticipates that it will recover the entire carrying value of such investments and has determined that no other-than-temporary impairments associated with credit losses were required to be recognized during the six months ended December 31, 2015.

Contractual maturities of available-for-sale securities at December 31, 2015 were as follows (in thousands):

|                       | December 31, 2015 |                  |
|-----------------------|-------------------|------------------|
|                       | Amortized Cost    | Fair Value       |
| Due in 1 year or less | \$ 44,236         | \$ 44,181        |
| Due in 1-2 years      | 23,236            | 23,123           |
|                       | <u>\$ 67,472</u>  | <u>\$ 67,304</u> |

The following table summarizes the carrying values and estimated fair values of our short-term and long-term debt (in thousands):

|                                  | December 31, 2015 |                   | June 30, 2015     |                   |
|----------------------------------|-------------------|-------------------|-------------------|-------------------|
|                                  | Carrying Value    | Fair Value        | Carrying Value    | Fair Value        |
| 3.75% Convertible Notes          | \$ 96,551         | \$ 101,423        | \$ 93,739         | \$ 102,645        |
| 3.50% Convertible Notes          | 44,654            | 60,666            | 44,654            | 65,230            |
| 3.50% Series A Convertible Notes | 65,518            | 95,570            | 64,460            | 102,760           |
| <b>Total</b>                     | <b>\$ 206,723</b> | <b>\$ 257,659</b> | <b>\$ 202,853</b> | <b>\$ 270,635</b> |

The short-term and long-term debt is measured on a non-recurring basis using Level 2 inputs based upon observable inputs of the Company's underlying stock price and the time value of the conversion option, since an observable quoted price of the Convertible Notes is not readily available.

## 5. Commitments and Contingencies

The Company's contractual obligations were presented in the Annual Report on Form 10-K for the previous annual reporting period ended June 30, 2015. There have been no material changes outside of the ordinary course of business in those obligations during the three months ended December 31, 2015.

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### Litigation

From time to time, the Company is involved in legal proceedings arising in the ordinary course of its business. The Company records a provision for a loss when it believes that it is both probable that a loss has been incurred and the amount can be reasonably estimated. Currently, management believes the Company does not have any probable and estimable losses related to any current legal proceedings and claims. Although occasional adverse decisions or settlements may occur, except as described in the matters below, management does not believe that an adverse determination with respect to any of these claims would individually or in the aggregate materially and adversely affect the Company's financial condition or operating results. For certain legal proceedings, management believes that there is a reasonable possibility that material losses may be incurred; however, the Company is unable to reasonably estimate a range of reasonably possible losses with respect to these matters. Litigation is inherently unpredictable and is subject to significant uncertainties, some of which are beyond the Company's control. Should any of these estimates and assumptions change or prove to have been incorrect, the Company could incur significant charges related to legal matters that could have a material impact on its results of operations, financial position and cash flows.

### Rotary Systems

On April 28, 2011, a former supplier to TomoTherapy, Rotary Systems Incorporated ("Rotary Systems"), filed suit in Minnesota state court, Tenth Judicial District, Anoka County, against TomoTherapy alleging misappropriation of trade secrets, as well as several other counts alleging various theories of injury. Rotary Systems alleges TomoTherapy misappropriated Rotary Systems' trade secrets pertaining to a component previously purchased from Rotary Systems, which TomoTherapy now purchases from a different supplier. The suit alleges TomoTherapy improperly supplied the alleged trade secrets to its present supplier, Dynamic Sealing Technologies Inc. (also a named defendant in the suit). Rotary Systems has made an unspecified claim for damages of greater than \$50,000. TomoTherapy moved to dismiss the case and, on August 29, 2011, the court granted the motion to dismiss with respect to all counts other than the count alleging misappropriation of trade secrets. On May 21, 2012, the court gave Rotary Systems sixty days to identify the alleged trade secrets with specificity or face dismissal of its claim with prejudice. The court held a hearing on September 20, 2012 to review Rotary Systems' amended

complaint. TomoTherapy filed a motion for summary judgment on the trade secret claim, the court ruled in favor of TomoTherapy on December 5, 2013, and Rotary Systems appealed. On December 22, 2014, the Minnesota Court of Appeals reversed the district court's dismissal of Rotary Systems' trade secrets claim and remanded it to the district court but affirmed the dismissal of Rotary Systems' other claims. In late October 2015, a final scheduling order was confirmed for the remanded claims and the parties are currently in the process of conducting discovery.

### **Cowealth Medical**

On February 27, 2014, Cowealth Medical Holding Co., Ltd. ("Cowealth"), Accuray's former distributor in China, submitted a request for binding arbitration with the International Chamber of Commerce International Court of Arbitration ("ICC") alleging, among other matters, that Accuray breached its distributor agreement with Cowealth by wrongfully terminating Cowealth as its distributor and misappropriated certain of Cowealth's confidential information. Cowealth was seeking damages of approximately \$170.0 million and injunctive relief. Accuray filed counterclaims for damages of approximately \$35.0 million. Accuray's answer and counterclaim were submitted to the ICC on May 12, 2014, and Cowealth served its reply on June 27, 2014. A hearing was held in Hong Kong between January 26, 2015 and February 6, 2015. The parties filed closing submissions and reply closing submissions in March 2015. On October 29, 2015, the ICC ruled that Accuray was liable for certain damages and awarded Cowealth approximately \$3.4 million. On November 27, 2015, Cowealth applied for a correction to the award to revise the amount of damages upwards to approximately \$5.5 million. On January 21, 2016, the arbitrator granted Cowealth's application for a correction on the grounds that the original award amount was a clerical error on the part of the arbitrator. Interest on the final award amount will accrue at a rate of 5% per annum starting 30 days after the date the corrected award was issued until payment. Accordingly, management recorded a charge of \$3.4 million for the first fiscal quarter ending September 30, 2015, and an additional \$2.1 million for the second fiscal quarter ending December 30, 2015. The parties filed cost submissions and reply cost submissions in December 2015. The ICC will subsequently issue a separate ruling as to legal costs and associated expenses; however, management does not believe the likelihood of an award of legal fees to Cowealth is probable or estimable as of December 31, 2015, so no additional amount has been recorded. Prior to the ruling of the ICC, no accrual was established in the Company's consolidated financial statements because management did not believe the likelihood of an award of damages to Cowealth was probable or estimable. In addition, the Company won several of its counterclaims including the right to be assigned the existing service contracts between Cowealth and Accuray customers, transfer to Accuray any regulatory clearances, licenses or permits obtained and held for the purposes of selling the CyberKnife System in China and deliver any consigned parts in their possession.

### **Software License Indemnity**

Under the terms of the Company's software license agreements with its customers, the Company agrees that in the event the software sold infringes upon any patent, copyright, trademark, or any other proprietary right of a third-party, it will indemnify its

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customer licensees against any loss, expense, or liability from any damages that may be awarded against its customer. The Company includes this infringement indemnification in all of its software license agreements and selected managed services arrangements. In the event the customer cannot use the software or service due to infringement and the Company cannot obtain the right to use, replace or modify the license or service in a commercially feasible manner so that it no longer infringes, then the Company may terminate the license and provide the customer a refund of the fees paid by the customer for the infringing license or service. The Company has not recorded any liability associated with this indemnification, as it is not aware of any pending or threatened actions that represent probable losses as of December 31, 2015.

## **6. Share-Based Compensation**

The following table summarizes the share-based compensation charges included in the Company's condensed consolidated statements of operations and comprehensive loss (in thousands):

|                            | Three Months Ended December 31, |                 | Six Months Ended December 31, |                 |
|----------------------------|---------------------------------|-----------------|-------------------------------|-----------------|
|                            | 2015                            | 2014            | 2015                          | 2014            |
| Cost of revenue            | \$ 433                          | \$ 560          | \$ 822                        | \$ 955          |
| Research and development   | 622                             | 804             | 1,171                         | 1,698           |
| Selling and marketing      | 758                             | 835             | 1,402                         | 1,486           |
| General and administrative | 1,552                           | 1,655           | 2,484                         | 2,988           |
|                            | <u>\$ 3,365</u>                 | <u>\$ 3,854</u> | <u>\$ 5,879</u>               | <u>\$ 7,127</u> |

## **7. Debt**

### *3.75% Convertible Senior Notes due August 2016*

On August 1, 2011, the Company issued the 3.75% Convertible Notes to certain qualified institutional buyers, or QIBs. The 3.75% Convertible Notes were offered and sold to the QIBs pursuant to Rule 144A under the Securities Act of 1933, as amended (the "Securities Act"), or Rule 144A. The net proceeds from the \$100 million offering, after deducting the initial purchaser's discount and commission and the related offering costs, were approximately \$96.1 million. The offering costs and the initial purchaser's discount and commission (which are recorded in Other Assets) are both being amortized to interest expense using the effective interest method over five years. The 3.75% Convertible Notes bear interest at a rate of 3.75% per year, payable semi-annually in arrears in cash on February 1 and August 1 of each year, beginning on February 1, 2012. The 3.75% Convertible Notes will mature on August 1, 2016, unless earlier repurchased, redeemed or converted. A portion of these notes were redeemed in January 2016, as noted in Note 9 below.

The 3.75% Convertible Notes were issued under an Indenture between the Company and The Bank of New York Mellon Trust Company, N.A., as trustee. Holders of the 3.75% Convertible Notes may convert their 3.75% Convertible Notes at any time on or after May 1, 2016 until the close of business on the business day immediately preceding the maturity date. Prior to May 1, 2016, holders of the 3.75% Convertible Notes may convert their 3.75% Convertible Notes only under the following circumstances: (1) during any calendar quarter after the calendar quarter ending September 30, 2011, and only during such calendar quarter, if the closing sale price of the Company's common stock for each of 20 or more trading days in the 30 consecutive trading days ending on the last trading day of the immediately preceding calendar quarter exceeds 130% of the conversion price in effect on the last trading day of the immediately preceding calendar quarter; (2) during the five consecutive business days immediately after any five consecutive trading-day period (such five consecutive

trading-day period, the “Note Measurement Period”) in which the trading price per \$1,000 principal amount of 3.75% Convertible Notes for each trading day of that Note Measurement Period was equal to or less than 98% of the product of the closing sale price of shares of the Company’s common stock and the applicable conversion rate for such trading day; (3) if the Company calls any or all of the 3.75% Convertible Notes for redemption, at any time prior to the close of business on the business day immediately preceding the redemption date; or (4) upon the occurrence of specified corporate transactions as described in the Indenture. Upon conversion by holders of the 3.75% Convertible Notes, the Company will have the right to pay or deliver, as the case may be, cash, shares of common stock of the Company or a combination thereof, at the Company’s election. At any time on or prior to the 33rd business day immediately preceding the maturity date, the Company may irrevocably elect to (a) deliver solely shares of common stock of the Company in respect of the Company’s conversion obligation or (b) pay cash up to the aggregate principal amount of the 3.75% Convertible Notes to be converted and pay or deliver, as the case may be, cash, shares of common stock of the Company or a combination thereof in respect of the remainder, if any, of the Company’s conversion obligation in excess of the aggregate principal amount of the 3.75% Convertible Notes being converted. The initial conversion rate is 105.5548 shares of the Company’s common stock per \$1,000 principal amount of 3.75% Convertible Notes (which represents an initial conversion price of approximately \$9.47 per share of the Company’s common stock). The conversion rate, and thus the conversion price, are subject to adjustment as further described below.

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Holders of the 3.75% Convertible Notes who convert their 3.75% Convertible Notes in connection with a “make-whole fundamental change,” as defined in the Indenture, may be entitled to a make-whole premium in the form of an increase in the conversion rate. Additionally, in the event of a “fundamental change,” as defined in the Indenture, holders of the 3.75% Convertible Notes may require the Company to purchase all or a portion of their 3.75% Convertible Notes at a fundamental change repurchase price equal to 100% of the principal amount of 3.75% Convertible Notes, plus accrued and unpaid interest, if any, to, but not including, the fundamental change repurchase date.

Prior to the maturity date, the Company may redeem for cash all or a portion of the 3.75% Convertible Notes if the closing sale price of its common stock exceeds 130% of the applicable conversion price (the initial conversion price is approximately \$9.47 per share of common stock) of such 3.75% Convertible Notes for at least 20 trading days during any consecutive 30 trading-day period (including the last trading day of such period).

In accordance with ASC 470-20, *Debt with Conversion and Other Options*, the Company separately accounts for the liability and equity conversion components of the 3.75% Convertible Notes. The principal amount of the liability component of the 3.75% Convertible Notes was \$75.9 million as of the date of issuance based on the present value of its cash flows using a discount rate of 10%, our approximate borrowing rate at the date of the issuance for a similar debt instrument without the conversion feature. The carrying value of the equity conversion component was \$24.1 million. A portion of the initial purchaser’s discount and commission and the offering costs totaling \$0.9 million was allocated to the equity conversion component. The liability component is being accreted to the principal amount of the 3.75% Convertible Notes using the effective interest method over five years. A portion of these notes were repurchased in January 2016, please refer to Note 9 below.

*3.50% Convertible Senior Notes due February 2018*

In February 2013, the Company issued \$115.0 million aggregate principal amount of its 3.50% Convertible Notes to certain QIBs. The 3.50% Convertible Notes were offered and sold to the QIBs pursuant to Rule 144A. The net proceeds from the offering, after deducting the initial purchaser’s discount and commission and the related offering costs, were approximately \$110.5 million. The offering costs and the initial purchaser’s discount and commission (which are recorded in Other Assets) are both being amortized to interest expense using the effective interest method over five years. The 3.50% Convertible Notes bear interest at a rate of 3.50% per year, payable semi-annually in arrears in cash on February 1 and August 1 of each year, which began on August 1, 2013. The 3.50% Convertible Notes will mature on February 1, 2018, unless earlier repurchased, redeemed or converted.

In April 2014, through a series of transactions, the Company refinanced approximately \$70.3 million aggregate principal amount of the 3.50% Convertible Notes with approximately \$70.3 million aggregate principal amount of the Company’s new 3.50% Series A Convertible Senior Notes due 2018 (the “3.50% Series A Convertible Notes”).

The 3.50% Convertible Notes were issued under an Indenture between the Company and The Bank of New York Mellon Trust Company, N.A., as trustee. Holders of the 3.50% Convertible Notes may convert their 3.50% Convertible Notes at any time until the close of business on the business day immediately preceding the maturity date. The 3.50% Convertible Notes are convertible, as described below into common stock of the Company at an initial conversion rate equal to 187.6877 shares of common stock per \$1,000 principal amount of the 3.50% Convertible Notes, which is equivalent to a conversion price of approximately \$5.33 per share of common stock, subject to adjustment.

Holders of the 3.50% Convertible Notes who convert their 3.50% Convertible Notes in connection with a “make-whole fundamental change”, as defined in the Indenture, may be entitled to a make-whole premium in the form of an increase in the conversion rate. Additionally, in the event of a “fundamental change,” as defined in the Indenture, holders of the 3.50% Convertible Notes may require the Company to purchase all or a portion of their 3.50% Convertible Notes at a fundamental change repurchase price equal to 100% of the principal amount of 3.50% Convertible Notes, plus accrued and unpaid interest, if any, to, but not including, the fundamental change repurchase date.

In accordance with guidance in ASC 470-20, *Debt with Conversion and Other Options* and ASC 815-15, *Embedded Derivatives*, the Company determined that the embedded conversion components of the 3.50% Convertible Note do not require bifurcation and separate accounting. The remaining \$44.7 million principal amount of the 3.50% Convertible Note has been recorded in Long-term Debt on the consolidated balance sheet as of December 31, 2015.

*3.50% Series A Convertible Senior Notes due February 2018*

On April 17, 2014, the Company entered into note exchange agreements with certain holders (the “Participating Holders”) of the 3.50% Convertible Notes to refinance approximately \$70.3 million aggregate principal amount of the 3.50% Convertible Notes

with approximately \$70.3 million aggregate principal amount of the 3.50% Series A Convertible Notes. Pursuant to the note exchange agreements, the Company also paid the Participating Holders an aggregate of approximately \$0.4 million in cash in connection with such transactions. The principal amount of 3.50% Convertible Notes refinanced for each \$1,000 principal amount of the 3.50% Series A Convertible Notes was \$1,000 and the amount in cash paid per \$1,000 principal amount of such 3.50% Convertible Notes delivered was determined in individual negotiations between the Company and each Participating Holder. The Series A Convertible Notes have the same interest rate, maturity and other terms as the 3.50% Convertible Notes, except that the 3.50% Series A Convertible Notes are convertible into cash, shares of the Company's common stock or a combination of cash and shares of common stock, at the Company's option.

The 3.50% Series A Convertible Notes were issued under an Indenture between the Company and The Bank of New York Mellon Trust Company, N.A., as trustee. Holders of the 3.50% Series A Convertible Notes may convert their Securities at any time on or after November 1, 2017 until the close of business on the business day immediately preceding the maturity date. Prior to November 1, 2017, holders of the 3.50% Series A Convertible Notes may convert their Securities only under the following circumstances: (1) during any calendar quarter after the calendar quarter ending September 30, 2014, and only during such calendar quarter, if the closing sale price of the Company's common stock for each of 20 or more trading days in the 30 consecutive trading days ending on the last trading day of the immediately preceding calendar quarter exceeds 130% of the conversion price in effect on the last trading day of the immediately preceding calendar quarter; (2) during the five consecutive business days immediately after any five consecutive trading-day period (such five consecutive trading-day period, the "Note Measurement Period") in which the trading price per \$1,000 principal amount of 3.50% Series A Convertible Notes for each trading day of that Securities Measurement Period was equal to or less than 98% of the product of the closing sale price of shares of the Company's common stock and the applicable conversion rate for such trading day; or (3) upon the occurrence of specified corporate transactions as described in the Indenture. Upon conversion by holders of the 3.50% Series A Convertible Notes, the Company will have the right to pay or deliver, as the case may be, cash, shares of common stock of the Company or a combination thereof, at the Company's election. At any time on or prior to the 17th business day immediately preceding the maturity date, the Company may irrevocably elect to (a) deliver solely shares of common stock of the Company in respect of the Company's conversion obligation or (b) pay cash up to the aggregate principal amount of the 3.50% Series A Convertible Notes to be converted and pay or deliver, as the case may be, cash, shares of common stock of the Company or a combination thereof in respect of the remainder, if any, of the Company's conversion obligation in excess of the aggregate principal amount of the 3.50% Series A Convertible Notes being converted. The initial conversion rate is 187.6877 shares of the Company's common stock per \$1,000 principal amount of 3.50% Series A Convertible Notes (which represents an initial conversion price of approximately \$5.33 per share of the Company's common stock). The conversion rate, and thus the conversion price, are subject to adjustment as further described below.

Holders of the 3.50% Series A Convertible Notes who convert their Notes in connection with a "make-whole fundamental change", as defined in the Indenture, may be entitled to a make-whole premium in the form of an increase in the conversion rate. Additionally, in the event of a "fundamental change," as defined in the Indenture, holders of the 3.50% Series A Convertible Notes may require the Company to purchase all or a portion of their 3.50% Convertible Notes at a fundamental change repurchase price equal to 100% of the principal amount of the 3.50% Series A Convertible Notes, plus accrued and unpaid interest, if any, to, but not including, the fundamental change repurchase date.

In accordance with Accounting Standards Codification, or ASC 470-20, *Debt with Conversion and Other Options*, the Company separately accounts for the liability and equity conversion components of the 3.50% Series A Convertible Notes. The principal amount of the liability component of the 3.50% Series A Convertible Notes was \$62.5 million as of the date of issuance based on the present value of its cash flows using a discount rate of 7%, our approximate borrowing rate at the date of the issuance for a similar debt instrument without the conversion feature. The carrying value of the equity conversion component was \$7.9 million. In addition, the portion of the cash amount paid to the Participating Holders totaling \$0.4 million was allocated to the debt discount with the remaining \$47,000 to the equity component. The liability component is being accreted to the principal amount of the 3.50% Series A Convertible Notes using the effective interest method through the maturity in February 2018.

The following table presents the carrying values of all Convertible Notes as of December 31, 2015 (in thousands):

|  | 3.75% Notes | 3.50% Notes | 3.50% Series A<br>Notes | Total      |
|--|-------------|-------------|-------------------------|------------|
| Carrying amount of the equity conversion component | \$ 23,189   | \$ —        | \$ 7,844                | \$ 31,033  |
| Principal amount of the Convertible Notes          | \$ 100,000  | \$ 44,654   | \$ 70,346               | \$ 215,000 |
| Unamortized debt discount                          | (3,449)     | —           | (4,828)                 | (8,277)    |
| Net carrying amount                                | \$ 96,551   | \$ 44,654   | \$ 65,518               | \$ 206,723 |

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A summary of interest expense on the Convertible Notes is as follows (in thousands):

|   | Three months ended<br>December 31, |          | Six months ended<br>December 31, |          |
|---|------------------------------------|----------|----------------------------------|----------|
|   | 2015                               | 2014     | 2015                             | 2014     |
| Interest expense related to contractual interest coupon         | \$ 1,990                           | \$ 1,943 | \$ 3,935                         | \$ 3,886 |
| Interest expense related to amortization of debt discount       | 1,950                              | 1,782    | 3,870                            | 3,541    |
| Interest expense related to amortization of debt issuance costs | 368                                | 369      | 771                              | 732      |
|   | \$ 4,308                           | \$ 4,094 | \$ 8,576                         | \$ 8,159 |

## 8. Accumulated Other Comprehensive Loss

The components of accumulated other comprehensive loss consist of net loss, unrealized gains and losses on available-for-sale investments, changes in foreign currency exchange rate translation and net changes related to defined benefit pension plan. These components are excluded from earnings and reported as a component of stockholders' equity. The foreign currency translation adjustment results from those subsidiaries not using the United States dollar as their functional currency since the majority of their economic activities are primarily denominated in their applicable local currency. Accordingly, all assets and liabilities related to these operations are translated at the current exchange rates at the end of each period. The resulting cumulative translation adjustments are recorded directly to the accumulated other comprehensive loss account in stockholders' equity. Revenues and expenses are translated at average exchange rates in effect during the period.

The components of accumulated other comprehensive loss in the equity section of the balance sheets are as follows (in thousands):

|   | December 31,<br>2015 | June 30,<br>2015 |
|---|----------------------|------------------|
| Net unrealized loss on short-term investments | \$ (168)             | \$ (77)          |
| Cumulative foreign currency translation gain  | 442                  | 1,168            |
| Defined benefit pension obligation            | (1,517)              | (1,517)          |
| Accumulated other comprehensive loss          | <u>\$ (1,243)</u>    | <u>\$ (426)</u>  |

## 9. Subsequent Events

### *New Debt Financing*

On January 11, 2016, the Company closed a \$70.0 million straight debt financing agreement with Cerberus Business Finance, LLC, an affiliate of Cerberus Capital Management, L.P (the “Financing Agreement”). The net proceeds of the loan are required to be used, in addition to \$30.0 million of cash funded by the Company, to retire \$100.0 million of convertible notes at the earlier of August 2016 or when otherwise redeemed. This financing consists of a \$70.0 million first lien senior secured term loan with a 700 basis point margin and 1 percent LIBOR floor. The loan will be amortized at an effective rate of 5% annually with final payment due in 5 years and is subject to certain maintenance-based covenants. The covenants in the Financing Agreement include:

- Secured leverage — defines the maximum amount of secured leverage that can be on the Company’s books at a given point in time calculated by the total secured debt divided by the last twelve months’ adjusted EBITDA;
- Total leverage — defines the maximum amount of total leverage that can be on the Company’s books at a given point in time calculated by the total debt divided by the last twelve months’ adjusted EBITDA;
- Fixed Charge Coverage Ratio — designed to ensure that the Company’s cash fixed charges are met with adequate free cash flow based on a minimum coverage ratio to be set and maintained;
- Minimum EBITDA — defines the minimum amount of adjusted EBITDA the Company must maintain and generate;
- Maximum CapEx — defines how much cash the Company can use annually to pursue capital projects, purchase PP&E and other related activities during the life of the loan; and
- Affirmative and negative covenants — defining reporting requirements, subsidiary asset restrictions, dividend distribution and repayment requirements among other general requirements.

### *3.75% Convertible Senior Notes partial Repurchase*

In January 2016, the Company repurchased approximately \$63.4 million in aggregate principal amount of its 3.75% Convertible Senior Notes due August 2016 for \$66.6 million in cash. As \$63.4 million of the 3.75% Convertible Senior Notes were settled in cash, a total of 6.7 million potentially dilutive shares are no longer potentially outstanding from an EPS perspective, these shares were already noted in Note 1 above as being excluded due to being anti-dilutive in the current fiscal quarter of 2016. Following such transactions, approximately \$44.7 million aggregate principal amount of the 3.50% Convertible Notes, approximately \$36.6 million aggregate principal amount of the 3.75% Convertible Notes and approximately \$70.3 million of the 3.50% Series A Convertible Notes remained outstanding. The Company expects to record a charge in the third quarter of fiscal 2016 of approximately \$1.0 million associated with the repurchase of the notes.

### *Cowearth Medical Litigation*

In February of 2014, Cowearth submitted a request for binding arbitration with the ICC alleging, among other matters, that Accuray breached its distributor agreement with Cowearth by wrongfully terminating Cowearth as its distributor and misappropriated certain of Cowearth’s confidential information. Cowearth was seeking damages of approximately \$170.0 million and injunctive relief. On October 29, 2015, the ICC ruled that Accuray was liable for certain damages and awarded Cowearth approximately \$3.4 million, while denying Cowearth’s claim for injunctive relief.

On November 27, 2015, Cowearth applied for a correction to the award dated October 29, 2015, to revise the amount of damages upwards to approximately \$5.5 million from the previously issued award of \$3.4 million. On January 21, 2016, the arbitrator granted Cowearth’s application for a correction on the grounds that the original award amount was a clerical error on the part of the arbitrator. As the legal matter arose before December 31, 2015, management recorded the additional charge of \$2.1 million into accrued liabilities and general and administrative expenses. After the initial award assessment of \$3.4 million in October 2015, no additional accrual had been recorded in the Company’s consolidated financial statements because management did not believe the likelihood of an additional award of damages to Cowearth was probable or estimable. Under the terms of the ICC Rules of Arbitration all awards are binding and cannot be appealed by either party. Further issues relating to costs remain to be finalized in the arbitration, none of which will affect the binding outcome under the interim and corrected award. The ICC will subsequently issue a separate ruling as to legal costs and associated expenses; however, management does not believe the likelihood of an award of legal fees to Cowearth is probable or estimable as of the date of the financials, so no additional amount has been recorded.

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## Item 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

*The following discussion and analysis of our financial condition as of December 31, 2015 and results of operations for the three and six months ended December 31, 2015 and 2014 should be read together with our condensed consolidated financial statements and related notes included elsewhere in this report. Statements made in this Form 10-Q report that are not statements of historical fact are forward-looking statements and are subject to the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995. Forward-looking statements in this report relate, but are not limited, to: our future results of operations and financial position, including the sufficiency of cash resources and expected cash flows to fund future operations, including the next 12 months; our backlog and expectations regarding age-outs, cancellations of contracts and foreign currency impacts, the effects of our process improvements on age-outs, backlog and revenue; expected uses of cash during fiscal 2016; the anticipated drivers of our future capital requirements; the success of the MLC for the CyberKnife Systems, its impact on our business; our expectations regarding the factors that will impact long-term success, sales, competitive positioning and long-term success for our CyberKnife and TomoTherapy Systems; our belief that TomoTherapy Systems offer clinicians and patients significant benefits over other radiation therapy systems in the market; the anticipated risks associated with our foreign operations and fluctuations in the U.S. dollar and foreign currencies as well as our ability to mitigate such risks; the sufficiency of our cash, cash flow equivalents and investments to*

meet our anticipated cash needs for working capital and capital expenditures and our business strategy, plans and objectives. Forward-looking statements generally can be identified by words such as “anticipates,” “believes,” “estimates,” “expects,” “intends,” “plans,” “predicts,” “projects,” “may,” “will be,” “will continue,” “will likely result,” and similar expressions. Forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from expectations, including those risks discussed in this quarterly report, in particular under the heading “Risk Factors” in Part II, Item 1A as well as the risks detailed in Part I, Item 1A of the Company’s annual report on Form 10-K for fiscal year 2015, in Part II, Item 1A of the Company’s quarterly report on Form 10-Q for the quarter ended September 30, 2015 and other filings we make with the Securities and Exchange Commission. Forward-looking statements speak only as of the date the statements are made and are based on information available to the Company at the time those statements are made and/or management’s good faith belief as of that time with respect to future events. The Company assumes no obligation to update forward-looking statements to reflect actual performance or results, changes in assumptions or changes in other factors affecting forward-looking information, except to the extent required by applicable securities laws. Accordingly, investors should not place undue reliance on any forward-looking statements.

In this report, “Accuray,” the “Company,” “we,” “us,” and “our” refer to Accuray Incorporated and its subsidiaries.

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**Overview**

**Products and Markets**

We are a radiation oncology company that develops, manufactures, sells and supports precise, innovative treatment solutions which set the standard of care, with the aim of helping patients live longer, better lives. Our leading edge technologies, the CyberKnife® and TomoTherapy Systems®, are designed to deliver advanced radiation therapy including radiosurgery, stereotactic body radiation therapy, intensity modulated radiation therapy, image-guided radiation therapy and adaptive radiation therapy tailored to the specific needs of each patient. The CyberKnife and TomoTherapy Systems are complementary offerings serving separate patient populations treated by the same medical specialty, radiation oncology, with advanced capabilities that offer increased treatment flexibility to meet the needs of an expanding patient population.

The CyberKnife Systems are robotic systems designed to deliver radiosurgery treatments to cancer tumors anywhere in the body. The CyberKnife Systems are the only dedicated, full-body robotic radiosurgery systems on the market. Radiosurgery is an alternative to traditional surgery for tumors and is performed on an outpatient basis in one to five treatment sessions. It enables the treatment of patients who otherwise would not be treated with radiation, who may not be good candidates for surgery, or who desire non-surgical treatments. The use of radiosurgery with CyberKnife Systems to treat tumors throughout the body has grown significantly in recent years, but currently only a small portion of the patients who develop tumors treatable with CyberKnife Systems are treated with these systems. A determination of when it may or may not be appropriate to use a CyberKnife System for treatment is at the discretion of the treating physician and depends on the specific patient. However, the CyberKnife Systems are generally not used to treat (1) very large tumors, which are considerably wider than the radiation beam that can be delivered by CyberKnife Systems, (2) diffuse wide-spread disease, as is often the case for late stage cancers, because they are not localized (though CyberKnife Systems might be used to treat a focal area of the disease) and (3) systemic diseases, like leukemia and lymphoma, which are not localized to an organ, but rather involve cells throughout the body. The addition of the multi-leaf collimator, or InCise MLC, now makes it faster and more efficient to treat a wider range of tumor types with the CyberKnife M6, including larger tumors and those with multiple sites of disease.

Our CyberKnife M6 Series Systems have the option of: fixed collimator, iris collimator and/or InCise MLC. The InCise MLC is designed specifically for the M6 Series. With the addition of the InCise MLC, clinicians can deliver the same precise radiosurgery treatments they have come to expect with the CyberKnife System, faster and for a wider range of tumor types. The InCise MLC was commercially launched in the third fiscal quarter of 2015.

We believe the long term success of the CyberKnife Systems is dependent on a number of factors including the following:

- Continued adoption of our CyberKnife M6 Series Systems;
- Production and shipment of MLC that meets the standards that we, and our customers, expect in our products;
- Change in medical practice leading to utilization of stereotactic body radiosurgery more regularly as an alternative to surgery or other treatments;
- Greater awareness among doctors and patients of the benefits of radiosurgery with the CyberKnife Systems;
- Continued evolution in clinical studies demonstrating the safety, efficacy and other benefits of using the CyberKnife Systems to treat tumors in various parts of the body;
- Continued advances in our technology that improve the quality of treatments and ease of use of the CyberKnife Systems;
- Receipt of regulatory approvals in various countries which is expected to improve access to radiosurgery with the CyberKnife Systems in such countries;
- Medical insurance reimbursement policies that cover CyberKnife System treatments; and
- Our ability to expand sales of CyberKnife Systems in countries throughout the world.

The TomoTherapy Systems are advanced, fully integrated and versatile radiation therapy systems for the treatment of a wide range of cancer types. The TomoTherapy Systems are the only radiation therapy systems designed for image-guided intensity-modulated radiation therapy (IG-IMRT). The TomoTherapy H Series Systems come in configurations of TomoH™, TomoHD™ and

TomoHDA™. Based on a CT scanner platform, the systems provide continuous delivery of radiation from 360 degrees around the patient, or delivery from clinician-specified beam angles. These unique features, combined with daily 3D image guidance, enable physicians to deliver highly accurate, individualized dose distributions which precisely conform to the shape of the patient's tumor while minimizing dose to normal, healthy tissue, resulting in fewer side effects for patients. The TomoTherapy Systems are capable of treating all standard radiation therapy indications including breast, prostate, lung and head and neck cancers, in addition to complex treatments such as total marrow irradiation. Radiation therapy has been widely available and used in developed countries for decades, though many developing countries do not currently have a sufficient number of radiation therapy systems to adequately treat their domestic cancer patient populations. The number of radiation therapy systems in use and sold each year is currently many times larger than the number of radiosurgery systems. We believe the TomoTherapy Systems offer clinicians and patients significant benefits over other radiation therapy systems in the market. We believe our ability to capture more sales will be influenced by a number of factors including the following:

- Continued adoption of our TomoTherapy H Series Systems;
- Greater awareness among doctors and patients of the benefits of radiation therapy using TomoTherapy Systems;
- Advances in our technology which improve the quality of treatments and ease of use of TomoTherapy Systems;
- Greater awareness among doctors of the now-established reliability of TomoTherapy Systems; and
- Our ability to expand sales of TomoTherapy Systems in countries throughout the world.

### **Sale of Our Products**

Generating revenue from the sale of our systems is a lengthy process. Selling our systems, from first contact with a potential customer to a signed sales contract that meets our backlog criteria (as discussed below) varies significantly and generally spans six months to two years. The time from receipt of a signed contract to revenue recognition is governed generally by the time required by the customer to build, renovate or prepare the treatment room for installation of the system.

In the United States, we primarily market directly to customers, including hospitals and stand-alone treatment facilities, through our sales organization and we also market to customers through sales agents and group purchasing organizations. Outside the United States, we market to customers directly and through distributors and some sales agents. In addition to our offices in the United States, we have sales and service offices in many countries in Europe, Japan and other countries in Asia, South America, and throughout the world.

### ***Backlog***

For orders that cover both products and services, only the portion of the order that is recognizable as product revenue is reported as backlog. The portion of the order that is recognized as service revenue (for example, Post Contract Customer Support (PCS), installation, training and professional services) is not included in reported backlog. Product backlog totaled \$366.7 million as of December 31, 2015.

In order for the product portion of a CyberKnife or TomoTherapy System sales agreement to be counted as backlog, it must meet the following criteria:

- The contract is signed and properly executed by both the customer and us. A customer purchase order that is signed and incorporates the terms of our contract quote will be considered equivalent to a signed and executed contract;
- The contract is non-contingent - it either has cleared all its contingencies or contains no contingencies when signed;
- We have received a minimum deposit or a letter of credit; the sale is a direct channel sale to a government entity, or the product has shipped to a customer with credit sufficient to cover the minimum deposit;
- The specific end customer site has been identified by the customer in the written contract or written amendment;
- For orders in our Latin America region, unless the system has already shipped and collection is reasonably assured, we request supporting evidence that the end customer has commenced construction to place our products if a site does not already exist; and

- Less than 2.5 years have passed since the contract met all the criteria above.

Although our backlog includes only contractual agreements with our customers for the purchase of CyberKnife Systems, TomoTherapy Systems and related upgrades, due to factors outside of our control, we cannot provide assurance that we will convert backlog into recognized revenue. The amount of backlog recognized into revenue is primarily impacted by three items: cancellations, age-outs and foreign currency fluctuations. Orders could be cancelled for reasons including, without limitation, changes in customers' needs or financial condition, changes in government or health insurance reimbursement policies, changes to regulatory requirements, or other reasons. In addition to cancellations, after 2.5 years, if we have not been able to recognize revenue on a contract, we remove the revenue associated with the contract from backlog and the order is considered aged out. Contracts may age-out for many reasons, including inability of the customer to pay, inability of the customer to adapt their facilities to accommodate our products in a timely manner, inability to timely obtain licenses necessary for customer facilities or operation of our equipment among other reasons for delays. Our backlog also includes amounts not denominated in U.S. Dollars and therefore fluctuations in the U.S. Dollar as compared to other currencies will impact backlog. Generally, strengthening in the U.S. Dollar will negatively impact backlog.

Gross orders are defined as the sum of new orders recorded during the period adjusted for any revisions to existing orders during the period. Net product orders are defined as gross product orders less cancellations, age-outs and foreign exchange adjustments.

| (Dollars in thousands)                 | Three months ended<br>December 31, |         |      | Six months ended<br>December 31, |    |         |    |         |
|--|------------------------------------|---------|------|----------------------------------|----|---------|----|---------|
|  | 2015                               |         | 2014 | 2015                             |    | 2014    |    |         |
| Gross orders                           | \$                                 | 67,078  | \$   | 72,261                           | \$ | 132,006 | \$ | 131,024 |
| Net orders                             |                                    | 42,679  |      | 41,474                           |    | 87,478  |    | 73,756  |
| Order backlog at the end of the period |                                    | 366,668 |      | 357,831                          |    | 366,668 |    | 357,831 |

Gross orders decreased by \$5.2 million for the three months ended December 31, 2015, as compared to the three months ended December 31, 2014. This was a result of a decrease of \$4.2 million in new system order volume added as the total number of system orders decreased from the same prior year period. The TomoTherapy System order volume decreased in this period partially offset by an increase in orders for the CyberKnife System fueled by the demand for the MLC, introduced in the third quarter of fiscal 2015. The remaining change was a result of fewer upgrade orders added in the three months ended December 31, 2015 as compared to the same prior year period.

Gross orders increased by \$1.0 million for the six months ended December 31, 2015, as compared to the six months ended December 31, 2014. This was a result of increased CyberKnife System order volume as compared to the same prior year period, partially offset by a slight decrease in TomoTherapy System order volume. The increase in CyberKnife System orders is in line with of the increased demand for systems with the MLC, after its introduction in the third quarter of fiscal 2015. The majority of new orders added for CyberKnife Systems this period were for systems with the MLC.

Net orders increased by \$1.2 million for the three months ended December 31, 2015, as compared to the three months ended December 31, 2014, resulting from \$3.9 million of fewer cancellations and more favorable currency impact causing an increase of \$3.4 million compared to the same period in prior year. These increases were partially offset by the decrease in gross orders of \$5.2 million and a slight increase in age-outs of \$0.9 million as compared to the same period in the prior year.

- Age-outs were \$19.1 million and \$18.1 million in the three months ended December 31, 2015 and 2014, respectively. The age-outs of \$19.1 million for the three months ended December 31, 2015 resulted from the age-out of two additional systems as compared to the prior year period.
- Cancellations were \$3.0 million and \$6.9 million in the three months ended December 31, 2015 and 2014, respectively. Cancellations are outside of our control and difficult to forecast; however, we continue to work closely with our customers to minimize the impact of cancellations on our business.
- Currency impacts resulted in decreases in net orders of \$2.3 million and \$5.8 million in the three months ended December 31, 2015 and 2014, respectively.

Net orders increased by \$13.7 million for the six months ended December 31, 2015, as compared to the six months ended December 31, 2014, resulting from the increase in gross orders of \$1.0 million plus an increase of \$10.8 million due to foreign currency impacts and an increase of \$3.5 million due to fewer cancellations. These increases were partially offset by higher age-outs resulting in a decrease of \$1.6 million.

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- Age-outs were \$37.5 million and \$35.9 million in the six months ended December 31, 2015 and 2014, respectively. The age-outs of \$37.5 million for the six months ended December 31, 2015 include \$5.3 million of age-ins which represent orders that previously aged-out but have been taken to revenue in the current period. There were no age-ins included in the age-out number for the six months ended December 31, 2014.
- Cancellations were \$6.0 million and \$9.5 million in the six months ended December 31, 2015 and 2014, respectively. Cancellations are outside of our control and difficult to forecast; however, we continue to work closely with our customers to minimize the impact of cancellations on our business.
- Currency impacts resulted in decreases in net orders of \$1.1 million and \$11.9 million in the three months ended December 31, 2015 and 2014, respectively.

Currently, we expect age-outs in the third quarter of this fiscal year to be in the range of \$5.0 to \$8.0 million as compared to \$11.6 million in age-outs recorded during the three months ended March 31, 2015. Between fiscal 2013 and 2015, we made changes to our order taking process, including increased oversight responsibility for and management of distributors and changes in timing as to when we enter some of our distributor orders into backlog. We believe these changes will improve the quality of backlog over time and reduce the level of age-outs.

## Results of Operations — Three and six months ended December 31, 2015 and 2014

| (Dollars in thousands)              | Three Months Ended December 31, |       |            |       |                       |             | Six Months Ended December 31, |             |       |                       |  |  |
|-------------------------------------|---------------------------------|-------|------------|-------|-----------------------|-------------|-------------------------------|-------------|-------|-----------------------|--|--|
|                                     | 2015                            |       | 2014       |       | 2015-2014<br>% change | 2015        |                               | 2014        |       | 2015-2014<br>% change |  |  |
|                                     | Amount                          | % (a) | Amount     | % (a) |                       | Amount      | % (a)                         | Amount      | % (a) |                       |  |  |
| Products                            | \$ 55,759                       | 51%   | \$ 47,650  | 49%   | 17%                   | \$ 95,754   | 48%                           | \$ 80,665   | 45%   | 19%                   |  |  |
| Services                            | 53,153                          | 49    | 50,505     | 51    | 5                     | 102,789     | 52                            | 99,871      | 55    | 3                     |  |  |
| Net revenue                         | \$ 108,912                      | 100%  | \$ 98,155  | 100%  | 11%                   | \$ 198,543  | 100%                          | \$ 180,536  | 100%  | 10%                   |  |  |
| Gross profit                        | \$ 42,571                       | 39%   | \$ 38,489  | 39%   | 11%                   | \$ 76,469   | 39%                           | \$ 66,290   | 37%   | 15%                   |  |  |
| Products gross profit               | 23,042                          | 41    | 20,479     | 43    | 13                    | 40,020      | 42                            | 32,829      | 41    | 22                    |  |  |
| Services gross profit               | 19,529                          | 37    | 18,010     | 36    | 8                     | 36,449      | 35                            | 33,461      | 34    | 9                     |  |  |
| Research and development expenses   | 14,931                          | 14    | 13,917     | 14    | 7                     | 29,227      | 15                            | 28,066      | 16    | 4                     |  |  |
| Selling and marketing expenses      | 15,076                          | 14    | 15,802     | 16    | (5)                   | 28,493      | 14                            | 33,776      | 19    | (16)                  |  |  |
| General and administrative expenses | 12,688                          | 12    | 12,361     | 13    | 3                     | 26,104      | 13                            | 23,311      | 13    | 12                    |  |  |
| Other expense, net                  | 5,070                           | 5     | 5,528      | 6     | (8)                   | 10,161      | 5                             | 10,989      | 6     | (8)                   |  |  |
| Provision for income taxes          | 833                             | 1     | 873        | 1     | (5)                   | 1,537       | 1                             | 1,790       | 1     | (14)                  |  |  |
| Net loss                            | \$ (6,027)                      | 6%    | \$ (9,992) | 10%   | (40)%                 | \$ (19,053) | 10%                           | \$ (31,642) | 18%   | (40)%                 |  |  |

(a) Expressed as a percentage of total net revenue, except for product and services gross profits which are expressed as a percentage of related product and services revenue.

## Net Revenue

*Product Net Revenue.* Product net revenue increased by \$8.1 million for the three months ended December 31, 2015, as compared to the three months ended December 31, 2014, primarily due to an increase of \$9.2 million in new system revenue due to an increase in the number of CyberKnife and TomoTherapy systems taken to revenue in the current period as compared to the prior year period. This increase was partially offset by a decrease of \$1.1 million in upgrade and other revenue as compared to the prior year period.

Product net revenue increased by \$15.1 million for the six months ended December 31, 2015, as compared to the six months ended December 31, 2014, primarily due to an increase of \$14.3 million in new system revenue due to an increase in the number of CyberKnife and TomoTherapy systems taken to revenue in the current period as compared to the prior year period. In addition, there was an increase of \$0.8 million in upgrade and other revenue as compared to the prior year period.

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*Services Net Revenue.* Services net revenue increased by \$2.6 million and \$2.9 million for the three and six months ended December 31, 2015, respectively, as compared to the three and six months ended December 31, 2014, respectively. The increase in services net revenue was primarily attributable to an increase in training revenue due to the timing of the expiration of training points; however, we don't expect training revenue from expired points to be at this volume going forward.

Percentage of net revenue by geographic region, based on the shipping location of our customers, is as follows (in thousands, except percentages):

|                                       | Three Months Ended<br>December 31, |           | Six Months Ended<br>December 31, |            |
|---------------------------------------|------------------------------------|-----------|----------------------------------|------------|
|                                       | 2015                               | 2014      | 2015                             | 2014       |
| Net revenue                           | \$ 108,912                         | \$ 98,155 | \$ 198,543                       | \$ 180,536 |
| Americas                              | 47%                                | 47%       | 48%                              | 47%        |
| Europe, Middle East, India and Africa | 14%                                | 27%       | 20%                              | 32%        |
| Asia (excluding Japan and India)      | 33%                                | 15%       | 27%                              | 11%        |
| Japan                                 | 6%                                 | 12%       | 5%                               | 11%        |

Revenue derived from sales outside of the Americas region was \$57.9 million and \$52.4 million for the three months ended December 31, 2015 and 2014, respectively, and represented 53% and 53% of our net revenue during these periods, respectively. Revenue derived from sales outside of the Americas region was \$102.3 million and \$96.3 million for the six months ended December 31, 2015 and 2014, respectively, and represented 51% and 53% of our net revenue during these periods.

## Gross Profit

Overall gross profit for the three months ended December 31, 2015, increased \$4.1 million, or 11%, as compared to the three months ended December 31, 2014. Product gross profit increased 13%, or \$2.6 million, primarily due to the increase in systems taken to revenue resulting in a higher profit margin due to increased leveraging of certain fixed costs. Service gross profit increased 8%, or \$1.5 million, as a result of higher service revenues of \$2.6 million driven by increased training revenue, partially offset by higher service costs of \$1.1 million mainly due to higher part consumption as compared to prior fiscal year.

Overall gross profit for the six months ended December 31, 2015, increased \$10.2 million, or 15%, as compared to the six months ended December 31, 2014. Product gross profit increased 22%, or \$7.2 million, primarily due to the increase in systems taken to revenue which resulted in a higher profit margin due to increased leverage of certain fixed costs. Service gross profit increased 9%, or \$3.0 million, as a result of higher service revenues of \$2.9 million driven by increased training revenue and lower service costs of \$0.1 million.

## Research and Development

Research and development expenses were \$14.9 million in the three months ended December 31, 2015 as compared to \$13.9 million in the three months ended December 31, 2014, which represents an increase of \$1.0 million, or 7%. The increase was primarily due to a \$1.5 million increase in consulting fees as a result of several new development projects that started in late fiscal 2015 and early fiscal 2016, partially offset by decreased compensation related expenses of \$0.5 million due to lower headcount as compared with the prior fiscal period.

Research and development expenses were \$29.2 million in the six months ended December 31, 2015 as compared to \$28.1 million in the six months ended December 31, 2014, which represents an increase of \$1.1 million, or 4%. The increase was primarily due to a \$3.1 million increase in consulting fees as a result of a development project that started in the third fiscal quarter of 2015. This increase was partially offset by decreased headcount related expenses of \$1.5 million due to lower headcount as compared with prior period and a decrease in materials and supplies expenses of \$0.5 million due to several large research and development projects completed prior to fiscal year 2016.

## Selling and Marketing

Selling and marketing expenses for the three months ended December 31, 2015 were \$15.1 million as compared to \$15.8 million for the three months ended December 31, 2014, which represents a decrease of \$0.7 million, or 4%. The decrease is primarily due to a \$1.4 million reduction in headcount related expense resulting mainly from a \$1.0 million reduction in commission expense due to several revenue deals with greater commission expense in the prior year as commission amount can vary from deal to deal and decreased salaries and benefits of \$0.4 million due to lower headcount. In addition there were decreased travel expenses of \$0.2 million also due to the lower headcount. These decreases were partially offset by an increase of \$0.9 million in marketing related

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expenses driven mainly by the timing and location of the ASTRO tradeshow which took place in the second fiscal quarter of 2016 whereas it took place in the first fiscal quarter of 2015.

Selling and marketing expenses for the six months ended December 31, 2015 were \$28.5 million as compared to \$33.8 million for the six months ended December 31, 2014, which represents a decrease of \$5.3 million, or 16%. The decrease is primarily due to a \$2.4 million reduction in headcount related expenses resulting mainly from lower commissions of \$1.5 million due to several revenue deals with greater commission expense in the prior year and decreased salaries and benefits of \$0.7 million related to lower headcount. Travel expenses also decreased by \$0.6 million due to lower headcount in the sales and marketing departments. General marketing expenses also decreased by \$0.9 million due to lower trade show expenses mainly for the ASTRO tradeshow due to location. In addition, consulting fees decreased by \$0.8 million due to fewer marketing initiative projects as compared to the prior year. Lastly, there were reductions of \$0.3 million in IT and facilities allocated expenses related to revised allocation rates and headcount in fiscal year 2016, and \$0.3 million reduction in general sales and marketing expenses related to software maintenance, business promotion and subscriptions.

### General and Administrative

General and administrative expenses for the three months ended December 31, 2015 were \$12.7 million as compared to \$12.4 million for the three months ended December 31, 2014, which represents an increase of \$0.3 million, or 3%. This increase was mainly attributable to higher legal fees associated with the additional Cowealth settlement in the second fiscal quarter of 2016 as described in Notes 5 and 9 to the financial statements.

General and administrative expenses for the six months ended December 31, 2015 were \$26.1 million as compared to \$23.3 million for the six months ended December 31, 2014, which represents an increase of \$2.8 million, or 12%. The increase was related to higher legal fees of \$2.7 million associated with the Cowealth settlement described in Note 5 to the financial statements. In addition, there were higher tax expenses of \$0.3 million due to several tax write-offs in prior year as well as higher bad debt expense of \$0.2 million resulting from bad debt recoveries in prior year; whereas, there were no similar offsetting tax write-offs or bad debt recoveries in the current fiscal year. These increases were partially offset by lower consulting expenses of \$0.4 million due to fewer projects with general and administrative involvement.

### Other Expense, net

Other expense, net for the three months ended December 31, 2015 was \$5.1 million as compared to \$5.5 million for the three months ended December 31, 2014, which represents a decrease of \$0.4 million, or 7%. Foreign currency losses decreased by \$1.1 million despite the fact that the U.S. Dollar continued to strengthen in comparison to the EURO, Japanese Yen and the Swiss Franc, because more sales agreements and related receivables outside of the U.S. were denominated in U.S. Dollar than in the same period of the previous year. This increase was partially offset by losses on hedging activities of \$0.5 million as compared to the same period in prior year due to increased hedging activities in the current year and month-to-month volatility of the Swiss Franc against the U.S. Dollar as well as higher interest expense of \$0.2 million due to continued debt discount accretion.

Other expense, net for the six months ended December 31, 2015 was \$10.2 million as compared to \$11.0 million for the six months ended December 31, 2014, which represents a decrease of \$0.8 million, or 7%. Foreign currency losses decreased by \$2.5 million despite the fact that the U.S. Dollar continued to strengthen in comparison to the EURO, Japanese Yen and the Swiss Franc, because more sales agreements and related receivables outside of the U.S. were denominated in U.S. Dollar than in the same period of the previous year. This increase was partially offset by losses on hedging activities of \$1.3 million as compared to the same period in prior year due to increased hedging activities in the current year and month-to-month volatility of the Swiss Franc against the U.S. Dollar as well as higher interest expense of \$0.4 million due to continued debt discount accretion.

### Provision for Income Taxes

On a quarterly basis, the Company provides for income taxes based upon an estimated annual effective income tax rate. Income tax expenses were \$0.8 million and \$1.5 million for the three and six months ended December 31, 2015, respectively, compared to income tax expenses of \$0.9 million and \$1.8 million for the three and six months ended December 31, 2014, respectively. The decrease in tax expense of \$0.1 million and \$0.3 million for the three and six months ended December 31, 2015, respectively, compared to the three and six months ended December 31, 2014 was primarily related to a decrease in earnings of our foreign subsidiaries.

### Liquidity and Capital Resources

At December 31, 2015, we had \$88.5 million in cash and cash equivalents and \$67.3 million in short-term investments, for a total of \$155.8 million. Refer to Note 7, "Debt" to the condensed consolidated financial statements for discussion of the Convertible Notes. Based on our current business plan and revenue prospects, we believe that we will have sufficient cash resources and anticipated cash flows to fund our operations for at least the next 12 months.

As of December 31, 2015, we had approximately \$55.3 million of cash and cash equivalents at our foreign subsidiaries. The earnings of our foreign subsidiaries are considered to be indefinitely reinvested outside the U.S. and unavailable for distribution in the form of dividends or otherwise. Accordingly, no provisions for U.S. income taxes have been provided thereon. We anticipate that we have adequate liquidity and capital resources for the next twelve months and do not anticipate the need to repatriate the undistributed earnings of our foreign subsidiaries at December 31, 2015.

Our cash flows for the six months ended December 31, 2015 and 2014 are summarized as follows (in thousands):

|  | <u>Six months ended December 31,</u> |             |
|--|--------------------------------------|-------------|
|  | <u>2015</u>                          | <u>2014</u> |
| Net cash provided by (used in) operating activities          | \$ 20,280                            | \$ (12,985) |
| Net cash (used in) provided by investing activities          | (7,750)                              | 21,239      |
| Net cash (used in) provided by financing activities          | (786)                                | 2,640       |
| Effect of exchange rate changes on cash and cash equivalents | (2,844)                              | (5,967)     |

**Cash Flows From Operating Activities**

Net cash provided by operating activities in the six months ended December 31, 2015 was \$20.3 million, as compared to \$13.0 million used in operating activities in the six months ended December 31, 2014. Net cash provided by operating activities in the six months ended December 31, 2015 was primarily related to:

- Net loss of \$19.1 million;
- Net loss was offset by non-cash items of \$21.0 million related to depreciation of fixed assets, amortization of intangible assets, share-based compensation, amortization and accretion of discount and premium on investments, amortization of debt issuance costs, accretion of interest on long-term debt, provision for doubtful accounts receivable and provision for excess and obsolete inventory;
- Decrease in restricted cash of \$1.0 million due to releases of restrictions on cash related to bunker constructions during the year;
- Decrease in accounts receivable of \$11.0 million as a result of collections on customer accounts in excess of billings resulting from significant sales transactions in the fourth fiscal quarter of 2015 that were collected in the first fiscal quarter of 2016, partially offset by a higher volume of invoicing as compared to payments in the second fiscal quarter of 2016;
- Increase in inventories of \$5.7 million due to increases in purchases in the first fiscal quarter of 2016 to support expected future sales and service needs that began to be utilized in the second fiscal quarter of 2016;
- Increase in prepaid expenses and other assets of \$3.6 million primarily due to an increase in long-term accounts receivable of \$6.5 million due to several large revenue contracts with extended payment terms. This was partially offset by a decrease of \$1.4 million due to the settlement of value-add taxes in foreign locations, reduction of other prepaids of \$0.7 million due to the release of vendor advances and amortization of prepayments for the ASTRO tradeshow offset by new additions, and a reduction in prepaid benefit costs of \$0.8 million due to the timing of payments;
- Increase in deferred revenue of \$5.9 million primarily due to additional product revenue deferrals added during the period in excess of the amount of deferred product revenue recognized;
- Increase in deferred cost of revenue of \$2.7 million primarily due to the timing of inventory transfers to customers;

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- Increase in accounts payable of \$6.7 million primarily due to an increase in inventory purchasing activities in the first half of fiscal 2016 and timing of payments as there was more large value payment activity at the end of prior year as compared with the end of the second fiscal quarter of 2016;
- Increase in accrued liabilities of \$5.4 million primarily related to an increase in legal accrual of \$5.7 million due to the award of damages related to the Cowealth litigation as described in Footnotes 5 and 9 to our consolidated financial statements as well as an increase in the bonus accrual of \$1.1 million for the first half of fiscal 2016. These increases were partially offset by decreased revenue related accruals of \$1.4 million due to the timing of payments; and
- Increase in customer advances of \$0.3 million due mainly to payments received for future revenue deliverables;

Net cash used in operating activities in the six months ended December 31, 2014 was primarily related to:

- Net loss of \$31.6 million;
- Net loss was offset by non-cash items of \$22.5 million related to depreciation of fixed assets, amortization of intangible assets, share-based compensation, amortization and accretion of discount and premium on investments, amortization of debt issuance costs, accretion of interest on long-term debt, recovery of doubtful accounts receivable and provision for excess and obsolete inventory;
- Decrease in accounts receivable of \$6.6 million as a result of collections on customer accounts in excess of billings;
- Increase in inventories of \$18.6 million due to increase in purchases to support expected future sales;
- Decrease in prepaid expenses and other assets of \$2.8 million primarily due to the reduction of prepaid taxes of \$1.8 million primarily in foreign locations due to settlements, a reduction in debt related costs of \$0.8 million due to continued amortization, and a decrease in prepaid commissions of \$0.5 million due to the conversion of deferred revenue into revenue in the second fiscal quarter of 2015. The decrease was offset by an increase in the prepaid insurance balance of \$0.5 million due to the timing of payments;
- Increase in deferred revenue of \$4.4 million primarily due the timing of service contract signing which resulted in more service contract deferrals as compared to prior period with a slight offset related to deferred system revenue which decreased due to additional installations of previously deferred systems;
- Decrease in deferred cost of revenue of \$1.9 million due to additional installations of previously deferred systems;
- Increase in accounts payable of \$1.3 million due to the timing of payments; and

- Decrease in accrued liabilities of \$3.1 million primarily related to the bonus accrual reduction of \$9.1 million due to bonus payments made in the first fiscal quarter of 2015 offset by additional accrual for bonuses for the six months ended December 31, 2014. This decrease was partially offset by an increase of \$3.7 million in deferred rent due to a renegotiated lease agreement, an increase of \$1.0 million in legal fees due to the timing of billings and payments for continued matters, and increases of \$0.6 million in interest payable and \$0.3 million in foreign taxes payable due to timing of payments.

## **Cash Flows From Investing Activities**

Net cash used in investing activities was \$7.7 million for the six months ended December 31, 2015, which primarily consisted of purchases of short-term investments of \$33.1 million and purchases of property and equipment of \$4.1 million partially offset by sales and maturities of investments of \$29.5 million.

Net cash provided by investing activities was \$21.2 million for the six months ended December 31, 2014, which primarily consisted of sales and maturities of short-term investments of \$81.4 million partially offset by purchases of property and equipment of \$4.2 million and purchases of investments of \$56.0 million.

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## **Cash Flows From Financing Activities**

Net cash used in financing activities during the six months ended December 31, 2015 was \$0.8 million from proceeds from employee stock plans offset by taxes paid related to net share settlement or equity awards. Net cash provided by financing activities during the six months ended December 31, 2014 was \$2.6 million from proceeds from employee stock plans.

## **Operating Capital and Capital Expenditure Requirements**

Our future capital requirements depend on numerous factors. These factors include but are not limited to the following:

- Revenue generated by sales of our products and service plans;
- Costs associated with our sales and marketing initiatives and manufacturing activities;
- Facilities, equipment and IT systems required to support current and future operations;
- Rate of progress and cost of our research and development activities;
- Costs of obtaining and maintaining FDA and other regulatory clearances of our products;
- Effects of competing technological and market developments; and
- Number and timing of acquisitions and other strategic transactions.

We believe that our current cash, cash equivalents and investments will be sufficient to meet our anticipated cash needs for working capital and capital expenditures for at least 12 months. If our cash and cash equivalents are insufficient to satisfy our liquidity requirements, we may seek to sell additional equity or debt securities or obtain additional credit facilities. The sale of additional equity or convertible debt securities could result in dilution to our stockholders. If additional funds are raised through the issuance of debt securities, these securities could have rights senior to those associated with our common stock and could contain covenants that would restrict our operations. Additional financing may not be available in amounts or on terms acceptable to us or at all. If we are unable to obtain this additional financing, we may be required to reduce the scope of our planned product development and marketing efforts.

## **Contractual Obligations and Commitments**

We presented our contractual obligations in our Annual Report on Form 10-K for the fiscal year ended June 30, 2015. There have been no material changes outside of the ordinary course of business in those obligations during the current quarter.

## **Off-Balance Sheet Arrangements**

We do not have any off-balance sheet arrangements.

## **Critical Accounting Policies and Estimates**

The discussion and analysis of our financial condition and results of operations is based on our condensed consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”). The preparation of these condensed consolidated financial statements requires management to make estimates and judgments that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements, as well as revenue and expenses during the reporting periods. We evaluate our estimates and judgments on an ongoing basis. We base our estimates on historical experience and on various other factors we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities. Actual results could therefore differ materially from those estimates if actual conditions differ from our assumptions.

During the six months ended December 31, 2015 we considered our estimated corporate bonus accrual to be a critical accounting estimate. The Company’s bonus accrual for each quarter is based on its performance against Company defined metrics: net revenue, adjusted EBITDA and gross orders to backlog. There have been no changes to the critical accounting policies and estimates, as discussed in Part II, Item 7 of our Form 10-K for the year ended

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**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

***Foreign Currency Exchange Rate Risk***

A portion of our net sales are denominated in foreign currencies, most notably the EURO and the Japanese Yen. Future fluctuations in the value of the U.S. dollar may affect the price competitiveness of our products outside the United States. For direct sales outside the United States, we sell in both U.S. dollars and local currencies, which could expose us to additional foreign currency risks. Our operating expenses in countries outside the United States are payable in foreign currencies and therefore expose us to currency risk, such as risks related to fluctuations in foreign currencies. To the extent that management can predict the timing of payments under sales contracts or for operating expenses that are denominated in foreign currencies, we may engage in hedging transactions to mitigate such risks in the future. We expect the changes in the fair value of the net foreign currency assets arising from fluctuations in foreign currency exchange rates to be materially offset by the changes in the fair value of the forward contracts. As of December 31, 2015, we had no open forward contracts and all open positions had been settled.

The purpose of these forward contracts is to minimize the risk associated with foreign exchange rate fluctuations. We have developed a foreign exchange policy to govern our forward contracts. These foreign currency forward contracts do not qualify as cash flow hedges and all changes in fair value are reported in earnings as part of other income and expenses. We have not entered into any other types of derivative financial instruments for trading or speculative purpose. Our foreign currency forward contract valuation inputs are based on quoted prices and quoted pricing intervals from public data and do not involve management judgment.

***Interest Rate Risk***

We maintain an investment portfolio of various holdings, types and maturities. These securities are generally classified as available for sale and consequently, are recorded on the balance sheet at fair value with unrealized gains and losses reported as a separate component of accumulated other comprehensive income. At any time, a sharp rise or decline in interest rates could have a material adverse impact on the fair value of our investment portfolio. Likewise, increases and decreases in interest rates could have a material impact on interest earnings for our portfolio. The following table presents the hypothetical change in fair values in the financial instruments we held at December 31, 2015 that are sensitive to changes in interest rates. The modeling technique used measures the change in fair values arising from selected potential changes in interest rates on our investment portfolio, which had a fair value of \$67.3 million at December 31, 2015. Market changes reflect immediate hypothetical parallel shifts in the yield curve of plus or minus 100, 75, 50 and 25 basis points (in thousands).

| Change in interest rate | Decrease in interest rates |         |         |         | Increase in interest rates |          |          |          |
|-------------------------|----------------------------|---------|---------|---------|----------------------------|----------|----------|----------|
|                         | -100 BPS                   | -75 BPS | -50 BPS | -25 BPS | 25 BPS                     | 50 BPS   | 75 BPS   | 100 BPS  |
| Unrealized gain (loss)  | \$ 442                     | \$ 348  | \$ 243  | \$ 123  | \$ (123)                   | \$ (247) | \$ (370) | \$ (494) |

***Equity Price Risk***

On August 1, 2011, we issued \$100 million aggregate principal amount of 3.75% Convertible Notes. Upon conversion, we can settle the obligation by issuing our common stock, cash or a combination thereof at an initial conversion rate equal to 105.5548 shares of common stock per \$1,000 principal amount of the 3.75% Convertible Notes, which is equivalent to a conversion price of approximately \$9.47 per share of common stock, subject to adjustment. There is no equity price risk if the share price of our common stock is below \$9.47 upon conversion of the 3.75% Convertible Notes. For every \$1 that the share price of our common stock exceeds \$9.47, we expect to issue an additional \$10.6 million in cash or shares of our common stock, or a combination thereof, if all of the 3.75% Convertible Notes are converted.

On April 24, 2014, we issued approximately \$70.3 million aggregate principal amount of 3.50% Series A Convertible Notes. Upon conversion, we can settle the obligation by issuing our common stock, cash or a combination thereof at an initial conversion rate equal to 187.6877 shares of common stock per \$1,000 principal amount of the 3.50% Series A Convertible Notes, which is equivalent to a conversion price of approximately \$5.33 per share of common stock, subject to adjustment. There is no equity price risk if the share price of our common stock is below \$5.33 upon conversion of the 3.50% Series A Convertible Notes. For every \$1 that the share price of our common stock exceeds \$5.33, we expect to issue an additional \$13.2 million in cash or shares of our common stock, or a combination thereof, if all of the 3.50% Series A Convertible Notes are converted.

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**Item 4. Controls and Procedures**

**Evaluation of Disclosure Controls and Procedures**

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow for timely decisions regarding required disclosure.

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of December 31, 2015. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that as of December 31, 2015 our disclosure controls and procedures were effective to provide reasonable assurance that the information required to be disclosed by us in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time

periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

#### *Changes in Internal Control Over Financial Reporting*

During the three months ended December 31, 2015, there was no change in our internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

#### *Inherent Limitations of Internal Control Over Financial Reporting*

Internal control over financial reporting cannot provide absolute assurance of achieving financial reporting objectives because of its inherent limitations. Internal control over financial reporting is a process that involves human diligence and compliance and is subject to lapses in judgment and breakdowns resulting from human failures. Internal control over financial reporting also can be circumvented by collusion or improper management override. Because of such limitations, there is a risk that material misstatements may not be prevented or detected on a timely basis by internal control over financial reporting. However, these inherent limitations are known features of the financial reporting process. Therefore, it is possible to design into the process safeguards to reduce, though not eliminate, this risk. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and in reaching a reasonable level of assurance, management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

## **PART II. OTHER INFORMATION**

### **Item 1. Legal Proceedings.**

Please refer to Note 5, Commitments and Contingencies, to the condensed consolidated financial statements above for a description of certain legal proceedings currently pending against the Company. From time to time we are involved in legal proceedings arising in the ordinary course of our business.

### **Item 1A. Risk Factors.**

A description of the risk factors associated with our business is included under "Risk Factors" contained in Part I, Item 1A of our Form 10-K for the year ended June 30, 2015, as updated in Part II, Item 1A of our quarterly report on Form 10-Q for the quarter ended September 30, 2015, and is incorporated herein by reference. The descriptions below include material changes to the risk factors affecting our business that were previously disclosed in such filings. Any risk factor included below supersedes the description of the relevant risk factor in such filings. Other than the items discussed below, there have been no material changes in our risk factors since such filings.

#### ***We have a large accumulated deficit, may incur future losses and may be unable to achieve profitability.***

As of December 31, 2015, we had an accumulated deficit of \$414.4 million. We may incur net losses in the future, particularly as we improve our selling and marketing activities. Our ability to achieve and sustain long-term profitability is largely dependent on our ability to successfully market and sell the CyberKnife and TomoTherapy Systems, control our costs and effectively

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manage our growth. We cannot assure you that we will be able to achieve profitability. In the event we fail to achieve profitability, our stock price could decline.

#### ***We have incurred significant indebtedness which imposes operating and financial restrictions on us which, together with our debt service obligations, could significantly limit our ability to execute our business strategy and increase the risk of default under our debt obligations.***

We borrowed an aggregate of approximately \$70 million pursuant to a term loan credit facility in January 2016. The terms of our credit facility require us to comply with certain financial maintenance covenants. In addition, the terms of our new indebtedness also include certain covenants restricting or limiting our ability to take certain actions. These covenants may adversely affect our ability to finance future operations, limit our ability to pursue certain business opportunities or take certain corporate actions. The covenants may also restrict our flexibility in planning for changes in our business and the industry and make us more vulnerable to economic downturns and adverse developments.

Our ability to meet our cash requirements, including our debt service obligations, will be dependent upon our operating performance, which will be subject to general economic and competitive conditions and to financial, business and other factors affecting our operations, many of which are or may be beyond our control. We cannot provide assurance that our business operations will generate sufficient cash flows from operations to fund these cash requirements and debt service obligations. If our operating results, cash flow or capital resources prove inadequate, we could face substantial liquidity problems and might be required to dispose of material assets or operations to meet our debt and other obligations. If we are unable to service our debt, we could be forced to reduce or delay planned expansions and capital expenditures, sell assets, restructure or refinance our debt or seek additional equity capital, and we may be unable to take any of these actions on satisfactory terms or in a timely manner. Further, any of these actions may not be sufficient to allow us to service our debt obligations or may have an adverse impact on our business. Our debt agreements limit our ability to take certain of these actions. Our failure to generate sufficient operating cash flow to pay our debts or to successfully undertake any of these actions could have a material adverse effect on us.

In addition, the degree to which we are leveraged as a result of the indebtedness incurred or otherwise could materially and adversely affect our ability to obtain additional financing for working capital, capital expenditures, acquisitions, debt service requirements or other purposes, could make us more vulnerable to general adverse economic, regulatory and industry conditions, could limit our flexibility in planning for, or reacting to, changes and opportunities in the markets in which we compete, could place us at a competitive disadvantage compared to our competitors that have less debt or could require us to dedicate a substantial portion of our cash flow to service our debt.

***As a strategy to assist our sales efforts, we may offer extended payment terms, which may potentially result in higher Days Sales Outstanding and greater payment defaults.***

We offer longer or extended payment terms for qualified customers in some circumstances. As of December 31, 2015, customer contracts with extended payment terms of more than one year amounted to 12% of our accounts receivable balance. While we qualify customers to whom we offer longer or extended payment terms, their financial positions may change adversely over the longer time period given for payment. This may result in an increase in payment defaults, which would affect our revenue, as we recognize revenue on such transactions on a cash basis.

***Our liquidity could be adversely impacted by adverse conditions in the financial markets.***

At December 31, 2015, we had \$88.5 million in cash and cash equivalents and \$67.3 million in investments. The available cash and cash equivalents are held in accounts managed by third-party financial institutions and consist of cash in our operating accounts and cash invested in money market funds. The investments are managed by third-party financial institutions and primarily consist of U.S. agency and corporate debt securities. We can provide no assurances that access to our invested cash and cash equivalents will not be impacted by adverse conditions in the financial markets.

At any point in time, we also have funds in our operating accounts that are with third-party financial institutions that exceed the Federal Deposit Insurance Corporation, or FDIC, insurance limits. While we monitor daily the cash balances in our operating accounts and adjust the cash balances as appropriate, these cash balances could be impacted if the underlying financial institutions fail or become subject to other adverse conditions in the financial markets. To date, we have experienced no loss or lack of access to cash in our operating accounts.

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***Our major stockholders own approximately 35.8% and directors and executive officers own approximately 2.6% of our outstanding common stock as of December 31, 2015, which could limit other stockholders' ability to influence the outcome of key transactions, including changes of control.***

As of December 31, 2015, our current holders of 5% or more of our outstanding common stock held in the aggregate approximately 35.8% of our outstanding common stock, while our directors and executive officers held in the aggregate approximately 2.6% of our outstanding common stock. This concentration of ownership may delay, deter or prevent a change of control of our company and will make some transactions more difficult or impossible without the support of these stockholders.

***Healthcare reform legislation could adversely affect demand for our products, our revenue and our financial condition.***

In March 2010, the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 were signed into law. The Affordable Care Act provides for, among other things, a 2.3% excise tax on U.S. sales of medical devices, including our products, which became effective in 2013. The excise tax was suspended for a two year period beginning January 1, 2016. This tax burden may have a material, negative impact on our business, results of operations and cash flow. In addition, these two pieces of legislation include a large number of other health related provisions, including expanding Medicaid eligibility, requiring most individuals to have health insurance, establishing new regulations on health plans, establishing health insurance exchanges, requiring manufacturers to report payments or other transfers of value made to physicians and teaching hospitals, modifying certain payment systems to encourage more cost-effective care and a reduction of inefficiencies and waste and including new tools to address fraud and abuse. The laws also include a decrease in the annual rate of inflation for Medicare payments to hospitals and the establishment of an independent payment advisory board to suggest methods of reducing the rate of growth in Medicare spending. There continue to be many programs and requirements for which the details have not yet been fully established or consequences not fully understood, and it is unclear what the full impact of the legislation will be.

In addition, since the adoption of the Affordable Care Act, other legislation designed to keep federal healthcare costs down has been proposed or passed. For example, under the sequestration required by the Budget Control Act of 2011, as amended by the American Taxpayer Relief Act of 2012, Medicare payments for all items and services under Parts A and B incurred on or after April 1, 2013 have been reduced by up to 2%. Future federal legislation may impose further limitations on the coverage or amounts of reimbursement available for our products from governmental agencies or third-party payors. These limitations could have a negative impact on the demand for our products and services, and therefore on our financial position and results of operations.

Future legislative or policy initiatives directed at reducing costs could be introduced at either the federal or state level. We cannot predict what healthcare reform legislation or regulations, if any, will be enacted in the United States or elsewhere, what impact any legislation or regulations related to the healthcare system that may be enacted or adopted in the future might have on our business, or the effect of ongoing uncertainty or public perception about these matters will have on the purchasing decisions of our customers. However, the implementation of new legislation and regulation may materially lower reimbursements for our products, materially reduce medical procedure volumes and significantly and adversely affect our business.

***Future issuances of shares of our common stock could dilute the ownership interests of our stockholders.***

Any issuance of equity securities could dilute the interests of our stockholders and could substantially decrease the trading price of our common stock. We may issue equity securities in the future for a number of reasons, including to finance our operations and business strategy (including in connection with acquisitions, strategic collaborations or other transactions), to adjust our ratio of debt to equity, to satisfy our obligations upon the exercise of outstanding options or for other reasons.

In August 2011, we issued \$100 million aggregate principal amount of our 3.75% Convertible Senior Notes due August 1, 2016 (the "3.75% Convertible Notes"), and in February 2013, we issued \$115 million aggregate principal amount of our 3.50% Convertible Senior Notes due February 1, 2018 (the "3.50% Convertible Notes"). In April 2014, we issued approximately \$70.3 million aggregate principal amount of our 3.50% Series A Convertible Senior Notes due February 1, 2018 (the "3.50% Series A Convertible Notes," and collectively with the 3.75% Convertible Notes and the 3.50% Convertible Notes, the "Convertible Notes") and paid approximately \$0.4 million in cash to refinance approximately \$70.3 million aggregate principal amount of our 3.50% Convertible Notes. In January 2016, we repurchased approximately \$63.4 million in aggregate principal amount of the 3.75% Convertible Notes for \$66.6 million in cash. Following such transactions, approximately \$44.7 million aggregate principal amount of the 3.50% Convertible Notes, approximately \$36.6 million aggregate principal amount of the 3.75% Convertible Notes and approximately \$70.3 million of the 3.50% Series A Convertible Notes remained outstanding. To the extent we issue common stock upon conversion of the Convertible Notes, that conversion would dilute the ownership interests of our stockholders.

***Increased leverage as a result of the Convertible Notes offering may harm our financial condition and operating results.***

As of December 31, 2015, we had total consolidated liabilities of approximately \$412.5 million, including the short-term liability component of the 3.75% Convertible Notes in the amount of \$96.6 million, and the long-term liability component of the 3.50% Convertible Notes in the amount of \$44.7 million and the 3.50% Series A Convertible Notes of \$65.5 million.

In April 2014, we refinanced approximately \$70.3 million aggregate principal amount of the 3.50% Convertible Notes held by certain investors (the “Participating Holders”) with approximately \$70.3 million aggregate principal amount of the 3.50% Series A Convertible Notes. In connection with such transactions, we also paid the Participating Holders approximately \$0.4 million in cash. In January 2016, we repurchased approximately \$63.4 million in aggregate principal amount of the 3.75% Convertible Notes for \$66.6 million in cash.

Our level of indebtedness could have important consequences to stockholders and note holders, because:

- It could affect our ability to satisfy our obligations under the Convertible Notes;
- A substantial portion of our cash flows from operations will have to be dedicated to interest and principal payments and may not be available for operations, working capital, capital expenditures, expansion, acquisitions or general corporate or other purposes;
- It may impair our ability to obtain additional financing in the future;
- It may limit our flexibility in planning for, or reacting to, changes in our business and industry; and
- It may make us more vulnerable to downturns in our business, our industry or the economy in general.

***Provisions in the indenture for the Convertible Notes, the loan credit facility, our certificate of incorporation and our bylaws could discourage or prevent a takeover, even if an acquisition would be beneficial in the opinion of our stockholders.***

Provisions of our certificate of incorporation and bylaws could make it more difficult for a third-party to acquire us, even if doing so would be beneficial in the opinion of our stockholders. These provisions include:

- authorizing the issuance of “blank check” preferred stock that could be issued by our board of directors to increase the number of outstanding shares and thwart a takeover attempt;
- establishing a classified board of directors, which could discourage a takeover attempt;
- prohibiting cumulative voting in the election of directors, which would limit the ability of less than a majority of stockholders to elect director candidates;
- limiting the ability of stockholders to call special meetings of stockholders;
- prohibiting stockholder action by written consent and requiring that all stockholder actions be taken at a meeting of our stockholders; and
- establishing advance notice requirements for nominations for election to the board of directors or for proposing matters that can be acted upon by stockholders at stockholder meetings.

In addition, Section 203 of the Delaware General Corporation Law may discourage, delay or prevent a change of control of our company. Generally, Section 203 prohibits stockholders who, alone or together with their affiliates and associates, own more than 15% of the subject company from engaging in certain business combinations for a period of three years following the date that the stockholder became an interested stockholder of such subject company without approval of the board or 66<sup>2</sup>/<sub>3</sub>% of the independent stockholders. The existence of these provisions could adversely affect the voting power of holders of common stock and limit the price that investors might be willing to pay in the future for shares of our common stock.

A change of control will also trigger an event of default under our term loan credit facility. If an event of default occurs, the collateral agent may, at its discretion, declare all or any portion of the loan then-outstanding under the loan credit facility, including all accrued but unpaid interest thereon, applicable fees and early payment premiums, to be accelerated and immediately due and payable.

Furthermore, if a “fundamental change” (as such terms are defined in each the indentures of the Convertible Notes) occurs, holders of the Convertible Notes will have the right, at their option, to require us to repurchase all or a portion of their Convertible Notes. A “fundamental change” generally occurs when there is a change in control of Accuray (acquisition of 50% or more of our voting stock, liquidation or sale of Accuray not for stock) or trading of our stock is terminated. In the event of a “make-whole fundamental change” (as such term is defined in each of the indentures for the Convertible Notes), we may also be required to increase the conversion rate applicable to the Convertible Notes surrendered for conversion in connection with such make-whole fundamental change. A “make-whole fundamental change” is generally a sale of Accuray not for stock in another publicly traded company. In addition, each of the indentures for the Convertible Notes prohibits us from engaging in certain mergers or acquisitions unless, among other things, the surviving entity assumes our obligations under the Convertible Notes.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

None.

**Item 3. Defaults Upon Senior Securities**

None.

**Item 4. Mine Safety Disclosures**

Not applicable.

**Item 5. Other Information**

None.

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| Exhibit No. | Exhibit Description  | Incorporated by Reference |           |         |                  | Filed Herewith |
|-------------|--|---------------------------|-----------|---------|------------------|----------------|
|             |  | Form                      | File No.  | Exhibit | Filing Date      |                |
| 10.1**      | Amended and Restated Executive Employment Agreement by and between Registrant and Kelly Lony, Dated October 15, 2015   | 8-K                       | 001-33301 | 10.1    | October 15, 2015 |                |
| 31.1        | Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended   | —                         | —         | —       | —                | X              |
| 31.2        | Certification of Chief Financial Officer Pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended   | —                         | —         | —       | —                | X              |
| 32.1*       | Certification of Chief Executive Officer and Chief Financial Officer Pursuant to Rule 13a-14(b) of the Securities Exchange Act of 1934, as amended, and 18 U.S.C. 1350 | —                         | —         | —       | —                |                |
| 101.INS     | XBRL Instance Document   |                           |           |         |                  | X              |
| 101.SCH     | XBRL Taxonomy Extension Schema Document  |                           |           |         |                  | X              |
| 101.CAL     | XBRL Taxonomy Extension Calculation Linkbase Document  |                           |           |         |                  | X              |
| 101.DEF     | XBRL Taxonomy Extension Definition Linkbase Document   |                           |           |         |                  | X              |
| 101.LAB     | XBRL Taxonomy Extension Label Linkbase Document  |                           |           |         |                  | X              |
| 101.PRE     | XBRL Taxonomy Extension Presentation Linkbase Document   |                           |           |         |                  | X              |

\*The certification attached as Exhibit 32.1 that accompanies this Quarterly Report on Form 10-Q is not deemed filed with the Securities and Exchange Commission and is not to be incorporated by reference into any filing of Accuray Incorporated under the Securities Act or the Securities Exchange Act of 1934, as amended, whether made before or after the date of this Quarterly Report on Form 10-Q, irrespective of any general incorporation language contained in such filing.

\*\* Management contract or compensatory plan or agreement.

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## SIGNATURES

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

ACCURAY INCORPORATED

By: /s/ Joshua H. Levine  
 Joshua H. Levine  
 President and Chief Executive Officer  
 (Principal Executive Officer)

By: /s/ Kevin M. Waters

Kevin M. Waters

Senior Vice President and Chief Financial Officer  
(Principal Financial Officer)

Date: February 1, 2016

**Certifications**

I, Joshua H. Levine, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Accuray Incorporated, a Delaware corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects, the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 1, 2016

/s/ Joshua H. Levine  
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Joshua H. Levine  
President and Chief Executive Officer  
(Principal Executive Officer)

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**Certifications**

I, Kevin M. Waters, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Accuray Incorporated, a Delaware corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects, the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 1, 2016

/s/ Kevin M. Waters

Kevin M. Waters

Senior Vice President and Chief Financial Officer  
(Principal Financial Officer)

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**Certification of Chief Executive Officer and Chief Financial Officer**

Pursuant to 18 U.S.C. § 1350, as created by Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned officers of Accuray Incorporated, a Delaware corporation (the “*Company*”) hereby certify, to such officers’ knowledge, that:

- (i) the accompanying Quarterly Report on Form 10-Q of the Company for the three months ended December 31, 2015 (the “*Report*”) fully complies with the requirements of Section 13(a) or Section 15(d), as applicable, of the Securities Exchange Act of 1934, as amended; and
- (ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: February 1, 2016

/s/ Joshua H. Levine

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Joshua H. Levine

President and Chief Executive Officer  
(Principal Executive Officer)

/s/ Kevin M. Waters

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Kevin M. Waters

Senior Vice President and Chief Financial Officer  
(Principal Financial Officer)

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