VICON INDUSTRIES INC /NY/
Form 10-Q
February 23, 2015

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

FORM 10-Q

S QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended December 31, 2014

£ 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: 1-7939

VICON INDUSTRIES, INC.
(Exact name of registrant as specified in its charter)

New York (State or other jurisdiction of incorporation or organization)	11-2160665 (I.R.S. Employer Identification No.)
135 Fell Court, Hauppauge, New York (Address of principal executive offices)	11788 (Zip Code)

(631) 952-2288
(Registrant’s telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x 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 ¨ (Do not check if a smaller reporting company)	Smaller reporting company x

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

At February 17, 2015, the registrant had outstanding 9,147,433 shares of Common Stock, $.01 par value.

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

VICON INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

	Three Months Ended	
	12/31/2014	12/31/2013
Net sales	$10,176,446	$8,109,194
Cost of sales	6,405,755	5,100,057
Gross profit	3,770,691	3,009,137
Operating expenses:		
Selling, general and administrative expense	4,297,889	3,267,296
Engineering and development expense	1,306,577	1,105,599
Restructuring charges	348,786	—
Merger and related expense	—	159,898
	5,953,252	4,532,793
Operating loss	(2,182,561)	(1,523,656)
Interest income	1,126	4,129
Loss before income taxes	(2,181,435)	(1,519,527)
Income tax expense	—	8,000
Net loss	$(2,181,435)	$(1,527,527)
Loss per share:		
Basic	$(.24)	$(.34)
Diluted	$(.24)	$(.34)
Weighted average shares outstanding:		
Basic	9,100,100	4,503,885
Diluted	9,100,100	4,503,885

See Accompanying Notes to Condensed Consolidated Financial Statements.

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VICON INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(UNAUDITED)

	Three Months Ended	
	12/31/2014	12/31/2013
Net loss	$(2,181,435)	$(1,527,527)
Other comprehensive income (loss):		
Unrealized gain (loss) on securities	1,349	(1,429)
Foreign currency translation adjustment	(145,229)	85,770
Other comprehensive income (loss)	(143,880)	84,341
Comprehensive loss	$(2,325,315)	$(1,443,186)

See Accompanying Notes to Condensed Consolidated Financial Statements.

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VICON INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

ASSETS	12/31/2014 (Unaudited)	9/30/2014
CURRENT ASSETS		
Cash and cash equivalents	$3,108,325	$4,751,270
Marketable securities	122,528	120,310
Accounts receivable, net	7,065,213	8,632,393
Inventories:		
Parts, components, and materials	2,016,397	1,491,835
Work-in-process	967,476	1,026,434
Finished products	6,983,271	6,309,986
	9,967,144	8,828,255
Prepaid expenses and other current assets	620,723	425,797
Assets held for sale	4,125,902	4,125,902
TOTAL CURRENT ASSETS	25,009,835	26,883,927
Property, plant and equipment	6,157,983	6,196,113
Less accumulated depreciation and amortization	(5,287,972)	(5,326,425)
	870,011	869,688
Goodwill	6,016,469	6,016,469
Intangible assets, net	3,926,667	4,034,667
Other assets	855,286	963,095
TOTAL ASSETS	$36,678,268	$38,767,846

LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable	$5,491,635	$5,441,528
Accrued compensation and employee benefits	2,650,652	2,984,554
Accrued expenses	1,753,994	2,095,135
Unearned revenue	974,665	357,597
TOTAL CURRENT LIABILITIES	10,870,946	10,878,814
Unearned revenue - non current	121,730	134,816
Other long-term liabilities	1,652,202	1,583,997
TOTAL LIABILITIES	12,644,878	12,597,627
Commitments and contingencies		
SHAREHOLDERS' EQUITY		
Common stock, par value $.01 per share		
authorized - 25,000,000 shares	100,036	99,008
issued - 10,003,631 and 9,900,868 shares		
Capital in excess of par value	40,731,686	40,544,228
Accumulated deficit	(12,314,108)	(10,132,673)
Treasury stock at cost, 856,198 shares	(4,226,852)	(4,226,852)

Accumulated other comprehensive loss	(257,372)	(113,492)
TOTAL SHAREHOLDERS' EQUITY	24,033,390	26,170,219
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$36,678,268	$38,767,846

See Accompanying Notes to Condensed Consolidated Financial Statements.

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VICON INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

	Three Months Ended	
	12/31/2014	12/31/2013
Cash flows from operating activities:		
Net loss	$(2,181,435)	$(1,527,527)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	151,870	101,130
Amortization of deferred compensation	1,202	1,202
Stock compensation expense	146,830	35,095
Change in assets and liabilities:		
Accounts receivable, net	1,500,845	2,091,236
Inventories, net	(1,192,025)	559,183
Prepaid expenses and other current assets	(201,526)	(55,714)
Other assets	107,809	4,049
Accounts payable	123,717	(603,203)
Accrued compensation and employee benefits	(320,922)	(696,266)
Accrued expenses	(332,293)	(84,031)
Unearned revenue	603,982	13,412
Other liabilities	71,220	24,288
Net cash used in operating activities	(1,520,726)	(137,146)
Cash flows from investing activities:		
Net increase in marketable securities	(869)	(767)
Capital expenditures	(48,833)	(13,910)
Net cash used in investing activities	(49,702)	(14,677)
Cash flows from financing activities:		
Proceeds from exercise of stock options	40,454	—
Net cash provided by financing activities	40,454	—
Effect of exchange rate changes on cash	(112,971)	29,124
Net decrease in cash	(1,642,945)	(122,699)
Cash and cash equivalents at beginning of year	4,751,270	8,281,714
Cash and cash equivalents at end of period	$3,108,325	$8,159,015

See Accompanying Notes to Condensed Consolidated Financial Statements.

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VICON INDUSTRIES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
December 31, 2014

Note 1: Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and the instructions to Form 10-Q and Rule 8-03 of Regulation S-X. Accordingly, they do not include all the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three months ended December 31, 2014 are not necessarily indicative of the results that may be expected for the fiscal year ended September 30, 2015. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's annual report on Form 10-K for the fiscal year ended September 30, 2014. Certain prior year amounts have been reclassified to conform to the current period presentation.

Note 2: Marketable Securities

Marketable securities consist of mutual fund investments principally in federal, state and local government debt securities of $122,528 as of December 31, 2014. Such mutual fund investments are stated at market value based on quoted market prices (Level 1 inputs) and are classified as available-for-sale under the provisions of Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 320, with unrealized gains and losses reported in accumulated other comprehensive income (loss) as a component of shareholders' equity. The cost of such securities at December 31, 2014 was $124,385, with $1,857 of cumulative unrealized losses reported at December 31, 2014.

Note 3: Accounts Receivable

Accounts receivable is stated net of an allowance for uncollectible accounts of $911,000 and $907,000 as of December 31, 2014 and September 30, 2014, respectively.

Note 4: Loss per Share

Basic loss per share (EPS) is computed based on the weighted average number of common shares outstanding for the period. Diluted EPS reflects the maximum dilution that would have resulted from incremental common shares issuable upon the exercise of stock options and under deferred compensation agreements.

The following tables provide the components of the basic and diluted EPS computations for the three month periods ended December 31, 2014 and 2013:

	Three Months Ended December 31,	
	2014	2013
Basic EPS Computation		
Net loss	$(2,181,435)	$(1,527,527)
Weighted average shares outstanding	9,100,100	4,503,885
Basic loss per share	$(.24)	$(.34)

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	Three Months Ended December 31, 2014	2013
Diluted EPS Computation		
Net loss	$(2,181,435)	$(1,527,527)
Weighted average shares outstanding	9,100,100	4,503,885
Stock options	—	—
Stock compensation arrangements	—	—
Diluted shares outstanding	9,100,100	4,503,885
Diluted loss per share	$(.24)	$(.34)

For the three months ended December 31, 2014 and 2013, all outstanding stock options and shares issuable under stock compensation arrangements totaling 686,858 and 445,820 shares, respectively, have been omitted from the calculation of diluted EPS as their effect would have been antidilutive. The actual effect of these stock options and shares, if any, on the diluted earnings per share calculation will vary significantly depending on fluctuations in the market price of the Company's stock.

Note 5: Accumulated Other Comprehensive Loss

The Company's accumulated other comprehensive loss balances at December 31, 2014 and September 30, 2014 consisted of the following:

	December 31, 2014	September 30, 2014
Foreign currency translation adjustment	$(255,515)	$(110,286)
Unrealized loss on marketable securities	(1,857)	(3,206)
Accumulated other comprehensive loss	$(257,372)	$(113,492)

Note 6: Goodwill and Intangible Assets

The Company’s goodwill balance of $6.0 million as of December 31, 2014 represents the excess of the purchase price over the fair value of net identifiable assets acquired in the August 29, 2014 IQinVision business combination (see Note 11). Goodwill is not amortized and is tested for impairment on an annual basis during the Company's fourth quarter, or more frequently if circumstances indicate impairment might exist. Goodwill is evaluated for impairment through the comparison of fair value of reporting units to their carrying values. When evaluating goodwill for impairment, the Company may first perform an assessment of qualitative factors to determine if the fair value of the reporting unit is more-likely-than-not greater than its carrying amount. This qualitative assessment is referred to as a "step zero" approach. If, based on the review of the qualitative factors, the Company determines it is not more-likely-than-not that the fair value of a reporting unit is less than its carrying value, the required two-step impairment test can be bypassed. If the Company does not perform a qualitative assessment or if the fair value of the reporting unit is not more-likely-than-not greater than its carrying value, the Company must perform the first step of the two-step impairment test, and calculate the estimated fair value of the reporting unit. If the carrying value of goodwill exceeds the estimated fair value, there is an indication that impairment may exist and the second step must be performed to measure the amount of impairment.

The amount of impairment is determined by comparing the implied fair value of the reporting unit goodwill to the carrying value of the goodwill in the same manner as if the reporting unit was being acquired in a business combination. If the implied fair value of goodwill is less than the recorded goodwill, an impairment loss for the difference would be recorded. In considering the step zero approach to testing goodwill for impairment, a qualitative analysis is performed evaluating factors including, but not limited to, macro-economic conditions, market and industry conditions, internal cost factors, competitive environment, share price fluctuations, results of past impairment tests, and the operational stability and the overall financial performance of the reporting units.

For the three months ended December 31, 2014, net sales from the Company's IQinVision business unit were below expectations and, accordingly, the Company has adjusted its sales forecast for this business unit for the balance of fiscal 2015. In addition, the

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Company's overall market capitalization has materially declined since this business combination. Such factors are indicators of potential goodwill impairment. However, due to the significant effort that is required to determine the implied fair value of a reporting unit's goodwill, we are unable to reasonably estimate the amount of goodwill impairment, if any, during the first quarter. The Company will conduct a formal impairment test prior to the required annual test in the second quarter, which may result in a material impairment charge.

Amortization is provided on a straight line method, or in the case of customer relationships, on an accelerated method. Following is a schedule of intangible assets, net:

	December 31, 2014	September 30, 2014	Estimated Useful Life
Definite-lived intangibles:			
Technology	$2,416,667	$2,479,167	10 years
Customer relationships	864,667	899,167	7 years
Tradenames	645,333	656,333	15 years
	$3,926,667	$4,034,667	

Amortization expense was $108,000 for the three months ended December 31, 2014. Future amortization expense for intangible assets over the next five years ending September 30 and thereafter is summarized as follows:

Fiscal Year	Amount
Remainder of 2015	$324,000
2016	517,000
2017	518,000
2018	427,000
2019	373,000
Thereafter	1,767,667

Note 7: Stock-Based Compensation

The Company maintains stock option plans that include both incentive and non-qualified options reserved for issuance to key employees, including officers and directors. All options are issued at fair market value at the grant date and are exercisable in varying installments according to the plans. The plans allow for the payment of option exercises through the surrender of previously owned mature shares based on the fair market value of such shares at the date of surrender.

The Company follows ASC 718 (“Share-Based Payment”), which requires that all share based payments to employees, including stock options, be recognized as compensation expense in the consolidated financial statements based on their grant date fair values and over the requisite service period. For the three month periods ended December 31, 2014 and 2013, the Company recorded non-cash compensation expense of $146,830 and $35,095, respectively ($.02 and $.01 per basic and diluted share, respectively), relating to stock compensation.

Note 8: Recent Accounting Pronouncements

In May 2014, the FASB issued guidance on revenue from contracts with customers. The underlying principle is that an entity will recognize revenue to depict the transfer of goods or services to customers at an amount that the entity expects to be entitled to in exchange for those goods or services. The guidance provides a five-step analysis of transactions to determine when and how revenue is recognized. Other major provisions include capitalization of certain contract costs, consideration of time value of money in the transaction price, and allowing estimates of variable consideration to be recognized before contingencies are resolved, in certain circumstances. The guidance also requires enhanced disclosures regarding the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers. This guidance permits the use of either the retrospective or cumulative effect transition method and is effective for the Company beginning in 2017; early adoption is not permitted. The Company has not yet evaluated the impact of this guidance on the Company's financial condition, results of operations and related disclosures.

In August 2014, the FASB issued guidance on management's responsibility in evaluating whether there is substantial doubt about a company's ability to continue as a going concern and related footnote disclosures. Management will be required to evaluate, at each reporting period, whether there are conditions or events that raise substantial doubt about a company's ability to continue as a going concern within one year from the date the financial statements are issued. This guidance is effective prospectively for annual and interim reporting period beginning in 2017. The Company has not yet evaluated the impact of this guidance on the Company’s financial condition, results of operations and related disclosures.

Note 9: Income Taxes

Deferred tax assets and liabilities are recognized based on the differences between the financial statement carrying amounts and the tax basis of assets and liabilities. Deferred tax assets represent items to be used as a tax deduction or credit in future tax returns for which a tax benefit has been recorded in the income statement. The Company has a valuation allowance against its deferred tax assets due to the uncertainty of future realization. The full valuation allowance is determined to be appropriate due to the Company's operating losses since fiscal year 2010 and the inherent uncertainties of predicting future operating results in periods over which such net tax differences become deductible. At September 30, 2014, the Company had $9.7 million of unrecognized net deferred tax assets available, which includes approximately $5.7 million of tax effected U.S. and foreign net operating loss carryforwards. On August 29, 2014, the Company merged with IQinVision, Inc. (see Note 11). In connection with this merger, the Company's ability to utilize pre-merger net operating losses and tax credit carryforwards in the future is subject to certain limitations pursuant to Section 382 of the Internal Revenue Code. No determination has been made at this time as to the occurrence of a Section 382 change in ownership. However, in such event, the annual limitation on utilization of the Company's U.S. net operating loss carryforwards is presently estimated at $500,000 based on a preliminary entity valuation.

The Company recognizes potential accrued interest and penalties related to unrecognized tax benefits in income tax expense. The Company files U.S. Federal and State income tax returns and foreign tax returns in the United Kingdom, Germany and Israel. The Company is generally no longer subject to tax examinations in such jurisdictions for fiscal years prior to 2011 in the U.S. and 2009 in the U.K., Germany and Israel.

Note 10: Fair Value

The majority of the Company’s non-financial assets and liabilities are not required to be carried at fair value on a recurring basis, but the Company is required on a non-recurring basis to use fair value measurements when analyzing asset impairment as it relates to long-lived assets. The carrying amounts for trade accounts and other receivables and accounts payable approximate fair value due to the short-term maturity of these instruments.

Fair value estimates are made at a specific point in time based on relevant market information about the financial instrument. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and, therefore, cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Note 11: Business Combination

On August 29, 2014, the Company merged with IQinVision, Inc. (“IQinVision”), a California corporation, with IQinVision surviving as a wholly owned subsidiary of the Company (the “Merger”). In connection with the Merger, the Company issued 4,522,335 shares of its common stock to IQinVision shareholders, which represented 50% of the Company’s outstanding common stock at the date of the Merger. In addition, the Company assumed a total of 642,420 of IQinVision stock options and stock appreciation rights along with related 2001 and 2011 Stock Incentive Plan provisions at the date of merger. The number and exercise prices of these equity instruments assumed were proportionately determined in accordance with a specified common stock exchange formula as to number and exercise price. The purchase price of the business combination at the date of closing was $14.9 million, consisting of 4,522,335 shares of Vicon common stock valued at $14.2 million on the date of issuance and assumed IQinVision stock options and stock appreciation rights valued at $723,000 in accordance with Financial Accounting Standards Board ASC 718. In connection with the Merger, the Company incurred $1.1 million of transaction and other merger related costs that were expensed in 2014 and, on September 12, 2014, paid a special cash dividend of $0.55 per share ($2.5 million in the aggregate) to Company shareholders of record as of July 11, 2014.

The Merger has been accounted for using the acquisition method of accounting and the Company has been treated as the acquirer for accounting purposes. This determination was made in accordance with the applicable accounting guidance based upon numerous factors including, but not limited to, the relative ownership of the combined company by the Company and former IQinVision shareholders, the composition of the management team and board of directors of the combined company, the structure of the Merger in which IQinVision became a wholly owned subsidiary of the Company, the location of the corporate offices of the combined company, and the continued listing of the Company's common stock on the NYSE MKT.

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The table below details the consideration transferred to acquire IQinVision:

	Conversion Calculation	Estimated Fair Value
Vicon Industries, Inc. shares of common stock issued at merger	4,522,335	
Per share price (ex-dividend) of Vicon Industries, Inc. common stock at August 29, 2014	$3.13	$14,154,909
Estimated fair value of vested IQinVision Stock Options assumed (1)		570,873
Estimated fair value of vested IQinVision SAR's assumed (1)		152,199
Estimated purchase price consideration		$14,877,981

(1) The fair value was determined using the Black-Scholes valuation model. Assumptions used are the same as those for acquired awards as disclosed in Note 1 of Notes to Consolidated Financial Statements.

The transaction has been accounted for using the acquisition method of accounting which requires that assets acquired and liabilities assumed be recognized at their fair values as of the acquisition date. The following table summarizes the allocation of the purchase price as of the acquisition date:

	August 29, 2014
Fair value of net assets acquired	$4,791,512
Intangible assets	4,070,000
Goodwill	6,016,469
Net assets acquired	$14,877,981

The following table is a summary of the fair value estimates of the identifiable intangible assets acquired and their useful lives:

	Useful Life (years)	Estimated Fair Value
Technology	10	$2,500,000
Customer relationships	7	910,000
Trademarks	15	660,000
		$4,070,000

Critical estimates in valuing certain intangible assets include but are not limited to estimating future expected cash flows from assets acquired and determining discount rates. Management’s estimates of fair value are based upon assumptions believed to be reasonable, but which are inherently uncertain and unpredictable and, as a result, actual results may differ from estimates. Estimates associated with the accounting for the acquisition may change as additional information becomes available.

The goodwill recognized is attributable primarily to expected synergies and other benefits that the Company believes will result from combining the operations of IQinVision with the operations of the Company. The $6.0 million goodwill that was acquired is not expected to be deductible for income tax purposes.

Note 12: Restructuring Charges

Pursuant to the August 29, 2014 IQinVision merger, the Company initiated certain integration and restructuring activities pursuant to an approved plan (the "Plan"). The Company recognized $349,000 of severance charges in the three months ended December 31, 2014 in connection with the Plan pursuant to notification of termination benefits to one affected employee.

Accounting for restructuring activities, as compared to regular operating cost management activities, requires an evaluation of formally committed and approved plans. Restructuring activities have comparatively greater strategic significance and materiality and may involve exit activities, whereas regular cost containment activities are more tactical in nature and are rarely characterized by formal and integrated action plans or exiting a particular product, facility or service.

Note 13: Product Warranties

The Company provides for the estimated cost of product warranties at the time revenue is recognized. While the Company engages in product quality programs and processes, including monitoring and evaluating the quality of its component suppliers, its warranty obligation is affected by product failure rates, material usage and service delivery costs incurred in correcting a product failure. Should actual product failure rates, material usage or service delivery costs differ from its estimates, revisions to the estimated warranty liability may be required.

Changes in the Company's warranty liability (included in accrued expenses) for the three months ended December 31, 2014 and 2013 were as follows and include the balances and activity of IQinVision, Inc. for periods subsequent to the merger date of August 29, 2014:

	Three Months Ended December 31,	
	2014	2013
Balance at beginning of year	$849,000	$411,000
Provision for warranties	128,000	11,000
Expenses incurred	(140,000)	(60,000)
Balance at end of period	$837,000	$362,000

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

General
Management's Discussion and Analysis of Financial Condition and Results of Operations discusses the Company's consolidated financial statements for the periods indicated, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. On an on-going basis, management evaluates its estimates and judgments, including those related to revenue recognition, bad debts, product warranties, inventories, long lived assets, goodwill, income taxes and contingencies and litigation. Management bases its estimates and judgments on historical experience and on various other factors including general market conditions that are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions. Results for the periods reported herein are not necessarily indicative of results that may be expected in future periods.

Overview
The Company designs, assembles and markets video management systems and system components for use in security, surveillance, safety and communication applications by a broad group of end users worldwide. The Company's product line consists of various elements of a video system, including DVR's, NVR's, video encoders, decoders, servers and related video management software, data storage units, analog, digital and HD megapixel fixed and robotic cameras, virtual and analog matrix video switchers and controls, and system peripherals.

The Company sells video surveillance system components in a highly competitive worldwide marketplace principally to authorized security dealers and system integrators. Such dealers and integrators typically resell and install the Company's products directly to end users, among other services. The Company's sales are principally project based and are largely dependent upon winning projects, construction activities and the timing of funding. Sales will vary from period to period depending upon many factors including seasonal and geographic trends in construction activities and the timing of deliveries due to changes in project schedules and funding. The Company usually does not have a large backlog as its customer orders are typically deliverable within three months or often upon receipt of order.

The Company competes in a market of rapid technology shifts which enhance the performance capability of security systems. As a result, the Company spends a significant amount on new product development. In fiscal 2014 and 2013, the Company incurred $4.6 million and $4.2 million of engineering and development expense or 13% and 11% of net sales, respectively. The Company's

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expenditures for product development are substantially less than its major competitors. The ongoing market shift to IP based products and network technologies will continue to burden the Company's development resources and increase ongoing annual expense for product development. Further, the Company's sales effort requires a high level of customer service and technical support for its products. The Company routinely considers various strategic options that may augment or supplement its present product offerings and technology platforms.

The Company has a foreign sales and distribution subsidiary in Europe that conducts business in British pounds and Euros that represented approximately 30% of the Company's consolidated sales for fiscal 2014. It also has an Israel based engineering and development subsidiary that incurs a majority of its operating expenses in Shekels that represented approximately 21% of the Company's operating expenses for fiscal 2014. The Company has historically entered into selected forward currency exchange contracts during favorable exchange rate conditions to help stabilize the impact of changing exchange rates and will consider doing so in the future, financing permitted. However, such hedging activities cannot entirely eliminate the long term effects of foreign currency exchange movements.

Business Combination

On August 29, 2014, the Company merged with IQinVision, Inc. ("IQinVision"), a California corporation, with IQinVision surviving as a wholly owned subsidiary of the Company (the "Merger"). In connection with the Merger, the Company issued 4,522,335 shares of its common stock to IQinVision shareholders, which represented 50% of the Company's outstanding common stock at the date of the Merger. In addition, the Company assumed a total of 642,420 IQinVision stock options and stock appreciation rights along with related 2001 and 2011 Stock Incentive Plan provisions at the date of merger. The number and exercise prices of these equity instruments assumed were proportionately determined in accordance with a specified merger agreement exchange formula. For accounting purposes, the purchase price of the business combination at the date of closing was $14.9 million, consisting of 4,522,335 shares of Vicon common stock valued at $14.2 million on the date of issuance and assumed IQinVision stock options and stock appreciation rights valued at $723,000 in accordance with Financial Accounting Standards Board ASC 718. In connection with the Merger, the Company incurred $1.1 million of transaction and other merger related costs that were expensed in fiscal 2014. Subsequent to the merger, the Company began execution of a global integration and restructuring plan ("the Plan") targeted to, among other things, reduce operating costs and maximize operating cash flow. The Company incurred certain related restructuring costs that have been reflected in its fiscal year 2014 and first quarter of fiscal 2015 results and anticipates incurring additional charges during at least the second quarter of fiscal year 2015 as planned initiatives are phased in.

In connection with the IQinVision merger, on September 12, 2014, the Company paid a special cash dividend of $0.55 per share ($2.5 million in the aggregate) to Company shareholders of record as of July 11, 2014.

The Merger has been accounted for using the acquisition method of accounting and the Company has been treated as the acquirer for accounting purposes. This determination was made in accordance with the applicable accounting guidance based upon numerous factors including, but not limited to, the relative ownership of the combined company by the Company and former IQinVision shareholders, the composition of the management team and board of directors of the combined company, the structure of the Merger in which IQinVision became a wholly owned subsidiary of the Company, the location of the corporate offices of the combined company, and the continued listing of the Company's common stock on the NYSE MKT.

The IQinVision product line augments the Company's OEM camera offerings and has historically been sold through many of the same market channels for use in similar end user applications.

Results of Operations
Three Months Ended December 31, 2014 Compared with December 31, 2013

Financial results for the three months ended December 31, 2014 include the full period results of operations for IQinVision due to the August 29, 2014 merger.

Net sales for the quarter ended December 31, 2014 increased by $2.1 million (25%) to $10.2 million compared with $8.1 million in the year ago period. Sales of IQinVision products for the current year quarter were $1.7 million. The Company's net sales for the first quarter of fiscal 2015, exclusive of IQinVision sales, increased by $390,000 (5%) compared with the year ago period. Sales in the Americas, exclusive of IQinVision, increased $1.3 million (26%) to $6.5 million compared with $5.1 million in the year ago period, while Europe, Middle East and Africa (EMEA) sales decreased $947,000 (32%) to $2.0 million compared with $3.0 million in the year ago period. Order intake for the quarter ended December 31, 2014 increased by $2.4 million (29%) to $10.6 million compared with $8.2 million in the year ago period. Orders of IQinVision products for the current year quarter were $1.6 million. North America order intake, exclusive of IQinVision, increased by $822,000 (15%) to $6.5 million compared with

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$5.7 million in the year ago period while EMEA order intake decreased 1% to $2.5 million compared with $2.6 million in the year ago period. The backlog of unfilled orders was $3.0 million at December 31, 2014 compared with $2.6 million at September 30, 2014.

Gross profit margins for each of the quarters ended December 31, 2014 and 2013 were 37.1%. Operating expenses for the quarter ended December 31, 2014 increased $1.4 million to $5.9 million compared with $4.5 million for the year ago period. Operating expenses of IQinVision for the current year quarter were $1.7 million. Operating expenses for the current year quarter, exclusive of IQinVision, decreased $294,000 principally as a result of reduced personnel costs. Selling, general and administrative (SG&A) expenses for the current quarter, which included $956,000 of IQinVision expenses, increased $1.0 million to $4.3 million compared with $3.3 million in the year ago period. Engineering and development expenses increased $201,000 to $1.3 million for the quarter ended December 31, 2014 compared with $1.1 million for the year ago period. Exclusive of $410,000 of IQinVision expenses, engineering and development expenses decreased $209,000 for the current quarter. In the current year quarter, the Company recognized $349,000 of severance charges in connection with a merger related integration and restructuring plan. Further restructuring charges are anticipated through at least the second quarter of fiscal 2015 as planned initiatives are phased in. In the year ago period, the Company incurred $160,000 of merger related costs in connection with the August 29, 2014 business combination.

The Company incurred an operating loss of $2.2 million for the first quarter of fiscal 2015 compared with an operating loss of $1.5 million in the year ago period. Excluding non-recurring restructuring charges of $349,000, the Company would have reported an operating loss of $1.8 million for the current quarter.

The Company recorded no income tax expense for the first quarter of fiscal 2015 compared with $8,000 in the year ago period. The year ago period amount represents minimum foreign subsidiary income taxes. The Company provides for a valuation allowance against its deferred tax assets due to the uncertainty of future realization and, thus, no tax benefit has been recognized on reported pretax losses for both periods (see Note 9: Income Taxes).

As a result of the foregoing, the Company reported a net loss of $2.2 million for the first quarter of fiscal 2015 compared with a net loss of $1.5 million in the year ago period.

Liquidity and Capital Resources

Net cash used in operating activities was $1.5 million for the first quarter of fiscal 2015. The Company incurred $1.9 million of cash operating losses for the period after $300,000 of non-cash charges. Such cash losses were offset in part by a $1.5 million reduction in accounts receivable, offset in part by a $1.2 million increase in inventories. Net cash used in investing activities was $50,000 for the first quarter of fiscal 2015 consisting principally of general capital expenditures. Net cash provided by financing activities was $40,000 for the first quarter of fiscal 2015 representing proceeds from the exercise of stock options. As a result of the foregoing, cash (exclusive of marketable securities) decreased by $1.6 million for the first quarter of fiscal 2015 after the effect of exchange rate changes on the cash position of the Company.

On August 29, 2014, the Company completed its merger with IQinVision, Inc. and subsequently began execution of a global integration and restructuring plan (the "Plan") targeted to, among other things, reduce operating costs and maximize operating cash flow. The Company incurred certain related restructuring costs that have been reflected in its first quarter of fiscal year 2015 results and anticipates incurring additional charges during at least the second quarter of fiscal year 2015 as planned initiatives are phased in. Pursuant to the Plan, in November 2014, the Company entered into a contract for the sale of its Edgewood, New York headquarters facility at a price of $3.5 million, excluding sales commission and closing costs. The transaction is expected to close in the second fiscal quarter of 2015 and is contingent upon certain buyer conditions and customary closing provisions. At the same time, the Company entered into a lease for a replacement headquarters facility located in Hauppauge, New York. The Company is also marketing its 14,000 square-foot United Kingdom based operating facility for sale, which is expected to be replaced by a smaller leased facility in the event of a sale transaction. These measures were taken in part to support anticipated cash flow requirements during 2015. These assets are presented as held for sale in the accompanying balance sheets.

The Company presently believes that it will have sufficient cash to meet its anticipated operating costs and capital expenditure requirements for at least the next twelve months based principally upon the receipt of proceeds associated with the anticipated closing of the Company's headquarters facility sale. In addition, the Company plans to explore third party financing sources. However, there is no assurance that such funding will be available.

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Off-Balance Sheet Arrangements

The Company does not have any off-balance sheet transactions, arrangements or obligations (including contingent obligations) that have, or are reasonably likely to have, a material effect on the Company’s financial condition, results of operations, liquidity, capital expenditures or capital resources.

Critical Accounting Policies

The Company's significant accounting policies are fully described in Note 1 to the Company's consolidated financial statements included in its September 30, 2014 Annual Report on Form 10-K. Management believes the following critical accounting policies, among others, affect its more significant judgments and estimates used in the preparation of its consolidated financial statements.

Revenue is generally recognized when products are sold and title is passed to the customer. Advance service billings are deferred and recognized as revenues on a pro rata basis over the term of the service agreement. Pursuant to Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 605-25-05, the Company evaluates multiple-element revenue arrangements for separate units of accounting, and follows appropriate revenue recognition policies for each separate unit. Elements are considered separate units of accounting provided that (i) the delivered item has stand-alone value to the customer, (ii) there is objective and reliable evidence of the fair value of the undelivered item, and (iii) if a general right of return exists relative to the delivered item, delivery or performance of the undelivered item is considered probable and substantially within the control of the Company. As applied to the Company, under arrangements involving the sale of product and the provision of services, product sales are recognized as revenue when the products are sold and title is passed to the customer, and service revenue is recognized as services are performed.

For products that include software and for separate licenses of the Company’s software products, the Company recognizes revenue in accordance with the provisions of FASB Accounting Standards Update (ASU) 2009-13, “Revenue Recognition (Topic 605) - Multiple-Deliverable Revenue Arrangements” (ASU 2009-13). ASU 2009-13 provides revenue recognition guidance for establishing separate units of accounting in a multiple element arrangement and requires the allocation of arrangement consideration to each deliverable in the arrangement based on the fair value of the elements. The fair value for each deliverable is based on vendor-specific objective evidence ("VSOE") if available, third-party evidence ("TPE") if VSOE is not available, or best estimate of selling price ("BESP") if neither VSOE nor TPE is available. BESP must be determined in a manner that is consistent with that used to determine the price to sell the specific elements on a standalone basis.

The Company maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. If the financial condition of its customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required.

The Company provides for the estimated cost of product warranties at the time revenue is recognized. While the Company engages in product quality programs and processes, including monitoring and evaluating the quality of its component suppliers, its warranty obligation is affected by product failure rates, material usage and service delivery costs incurred in correcting a product failure. Should actual product failure rates, material usage or service delivery costs differ from its estimates, revisions to the estimated warranty liability may be required.

The Company writes down its inventory for estimated obsolescence and slow moving inventory equal to the difference between the carrying cost of inventory and the estimated net realizable market value based upon assumptions about future demand and market conditions. Technology changes and market conditions may render some of the Company’s products obsolete and additional inventory write-downs may be required. If actual future demand or market conditions are less favorable than those projected by management, additional inventory write-downs may be required.

The Company evaluates the establishment of technological feasibility of its software in accordance with ASC 985 ("Accounting for the Costs of Computer Software to be Sold, Leased or Otherwise Marketed"). The Company has determined that technological feasibility for its new products is reached shortly before products are released for field testing. Costs incurred after technological feasibility has been established have not been material and are expensed as incurred.

The Company assesses the recoverability of the carrying value of its long-lived and intangible assets whenever events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. The Company evaluates the recoverability of such assets based upon the expectations of undiscounted cash flows from such assets. If the sum of the expected future undiscounted cash flows were less than the carrying amount of the asset, a loss would be recognized for the difference between the fair value and the carrying amount.

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The Company’s goodwill represents the excess of the purchase price over the fair value of net identifiable assets acquired in the recent business combination. Goodwill is not amortized and is tested for impairment at least annually. When evaluating goodwill for impairment, the Company may first perform an assessment of qualitative factors to determine if the fair value of the reporting unit is more-likely-than-not greater than its carrying amount. If, based on the review of the qualitative factors, the Company determines it is not more-likely-than-not that the fair value of a reporting unit is less than its carrying value, the required two-step impairment test can be bypassed. If the Company does not perform a qualitative assessment or if the fair value of the reporting unit is not more-likely-than-not greater than its carrying value, the Company must perform the first step of the two-step impairment test, and calculate the estimated fair value of the reporting unit. If the carrying value of goodwill exceeds the estimated fair value, there is an indication that impairment may exist and the second step must be performed to measure the amount of impairment loss. The amount of impairment for goodwill is measured as the excess of its carrying amount over its fair value. For the three months ended December 31, 2014, net sales from the Company's IQinVision business unit were below expectations and, accordingly, the Company has adjusted its sales forecast for this business unit for the balance of fiscal 2015. In addition, the Company's overall market capitalization has materially declined since this business combination. Such factors are indicators of potential goodwill impairment. However, due to the significant effort that is required to determine the implied fair value of a reporting unit's goodwill, we are unable to reasonably estimate the amount of goodwill impairment, if any, during the first quarter. The Company will conduct a formal impairment test prior to the required annual test in the second quarter, which may result in a material impairment charge.

The Company's ability to recover the reported amounts of deferred income tax assets is dependent upon its ability to generate sufficient taxable income during the periods over which net temporary tax differences become deductible. The Company provides for a valuation allowance against all deferred tax assets due to the uncertainty of future realization. The Company plans to provide a full valuation allowance against its deferred tax assets until such time that it can achieve a sustained level of profitability or other positive evidence arises that would demonstrate an ability to recover such assets.

The Company accrues liabilities for identified tax contingencies that result from positions that are being challenged or could be challenged by tax authorities. The Company believes that its accrual for tax liabilities is adequate for all open years, based on Management’s assessment of many factors, including its interpretations of the tax law and judgments about potential actions by tax authorities. However, it is possible that the ultimate resolution of any tax audit may be materially greater or lower than the amount accrued.

Accounting for restructuring activities, as compared to regular operating cost management activities, requires an evaluation of formally committed and approved plans. Restructuring activities have comparatively greater strategic significance and materiality and may involve exit activities, whereas regular cost containment activities are more tactical in nature and are rarely characterized by formal and integrated action plans or exiting a particular product, facility or service.

The Company is subject to proceedings, lawsuits and other claims related to labor, product and other matters. The Company assesses the likelihood of an adverse judgment or outcomes for these matters, as well as the range of potential losses. A determination of the reserves required, if any, is made after careful analysis. The required reserves may change in the future due to new developments.

Safe Harbor Statement under the Private Securities Litigation Reform Act of 1995

Statements in this Report on Form 10-Q that are not strictly historical facts including, without limitation, statements included under the “Management’s Discussion and Analysis” caption, are “forward-looking” statements within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, that should be considered as subject to the many risks and uncertainties that exist in the Company's operations and business environment. The forward-looking statements are based on current expectations and involve a number of known and unknown risks and uncertainties that could cause the actual results, performance and/or achievements of the Company to differ materially from any future results, performance or achievements, express or implied, by the forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements, and that in light of the significant uncertainties inherent in forward-looking statements, the inclusion of such statements should not be regarded as a representation by the Company or any other person that the objectives or plans of the Company will be achieved. The Company assumes no obligation to publicly update or revise its forward-looking statements or to advise of changes in the assumptions and factors on which they are based.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

The Company’s management, with the participation of its Chief Executive Officer and Chief Financial Officer, conducted an evaluation of the effectiveness of the design and operation of the Company’s disclosure controls and procedures, as required by Exchange Act Rule 13a-15. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of the period covered by this report, the Company’s disclosure controls and procedures were effective to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified by the Securities and Exchange Commission’s rules and forms and such information is accumulated and communicated to management as appropriate to allow timely decisions regarding required disclosures.

Changes in Internal Controls

There were no changes in the Company's internal control over financial reporting identified in connection with the evaluation referred to above that occurred during the quarter ended December 31, 2014 that have materially affected, or are reasonably likely to materially affect, the registrant's internal control over financial reporting.

PART II – OTHER INFORMATION

ITEM 1 - LEGAL PROCEEDINGS
None

ITEM 2 – UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

In December 2008, the Company’s Board of Directors authorized the purchase of up to $1 million worth of shares of the Company’s outstanding common stock. In December 2009, the Board of Directors authorized the purchase of an additional $1.5 million worth of shares of the Company’s outstanding common stock. The Company did not repurchase any of its common stock during the three month period ended December 31, 2014. The approximate dollar value of shares that may yet be purchased under the program was $972,679 as of December 31, 2014.

ITEM 3 - DEFAULTS UPON SENIOR SECURITIES
None

ITEM 4 – MINE SAFETY DISCLOSURES
Not applicable

ITEM 5 - OTHER INFORMATION
None

ITEM 6 – EXHIBITS

Exhibit Number	Description
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS	XBRL Instance Document*
101.SCH	XBRL Taxonomy Extension Schema Document*
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document*
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document*
101.LAB	XBRL Taxonomy Extension Label Linkbase Document*
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document*

*	In accordance with Regulation S-T, the XBRL-related information in Exhibit 101 to this Quarterly Report on Form 10-Q shall be deemed to be “furnished” and not “filed.”

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Signatures

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

VICON INDUSTRIES, INC.

February 23, 2015

/s/ Eric S. Fullerton	/s/ John M. Badke
Eric S. Fullerton	John M. Badke
Chief Executive Officer	Senior Vice President, Finance and Chief Financial Officer