EYE DYNAMICS INC
Form 10QSB
August 15, 2005

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

Form 10-QSB

(X) Quarterly Report under Section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended June 30, 2005

Commission File No. 0-27857

EYE DYNAMICS, INC.

(Name of small business issuer as specified in its charter)

Nevada	88-0249812
(State or other jurisdiction of incorporation)	(I.R.S. Employer Identification No.)

2301 W. 205th Street, #102, Torrance, CA 90501

(Address of principal executive offices)

310-328-0477

(Issuer's telephone number)

The number of shares outstanding of the issuer's common stock as of June 30, 2005 was 21,674,880.

Transitional Small Business Disclosure Format (check one) ( ) Yes; (X) No.

PART I. FINANCIAL INFORMATION

ASSETS

Current Assets	
Cash	$ 339,068
Certificate of deposits	400,000
Accounts receivable, net of allowance for bad debt of $899	157,333
Note receivable, net of allowance for loan losses of $67,334	9,115
Inventory	264,000
Prepaid expenses and taxes	21,515
TOTAL CURRENT ASSETS	1,191,031
Property and equipment, net of accumulated depreciation of $13,649	795
Other Assets	219,520

TOTAL ASSETS	$ 1,411,346

LIABILITIES AND STOCKHOLDERS' EQUITY

Current Liabilities	
Accounts payable	$ 39,989
Accrued expenses	26,517
TOTAL CURRENT LIABILITIES	66,506
Stockholders' Equity	
Common stock, $0.001 par value; 50,000,000 shares authorized; 21,674,880 shares issued and outstanding	21,674
Paid-in capital	3,607,618
Accumulated deficit	(2,284,452)
TOTAL STOCKHOLDERS' EQUITY	1,344,840
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 1,411,346

	FOR THREE MONTHS ENDED JUNE 30,		F E
	2005	2004	200
Sales - Products	$ 402,785	$ 456,581	$ 719
Cost of Products	187,283	213,451	337
Gross profit	215,502	243,130	382
Selling, general and administrative expenses	174,581	174,473	415
Operating income (loss)	40,921	68,657	(32
Other income(expenses)			
Interest and other income	128	-	
Interest expense	(194)	(921)	(1
Total other income (expenses)	(66)	(921)	
Net income (loss) before taxes	40,855	67,736	(33
Provision for income taxes	1,276	-	2
Net income (loss)	$ 39,579	$ 67,736	$ (35
Net income (loss) per share-basic	$ 0.00	$ 0.00	$ (

Net income (loss) per share-diluted	$ 0.00	$ 0.00	$ (
Shares used in per share calculation-basic	21,674,880	17,883,081	19,812
Shares used in per share calculation-diluted	22,179,707	21,763,168	19,812

FOR SIX MONTHS ENDED JUNE 30,	2005	20
CASH FLOW FROM OPERATING ACTIVITIES:		
Net income (loss)	$ (35,881)	$ 2
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation	80	
Provision for loan loss	9,116	
Issuance of stock for services	68,000	
(Increase) Decrease in:		
Accounts Receivable	(112,841)	(
Inventory	(83,292)	
Prepaid and Others	24,725	
Deferred Tax Asset	1,276	
Increase (Decrease) in:		
Accounts Payable and Accrued Expenses	19,150	(
NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	(109,667)	
CASH FLOW FROM INVESTING ACTIVITIES:		
Repayment from Notes Receivable	1,500	
Purchase of Certificate of Deposits	(400,000)	
Employee loan and advances	-	
NET CASH USED IN INVESTING ACTIVITIES	(398,500)	
CASH FLOW FROM FINANCING ACTIVITIES:		
Repayments on Notes Payable	-	(
NET CASH USED IN FINANCING ACTIVITIES	-	(
NET INCREASE (DECREASE) IN CASH	(508,167)	
CASH BALANCE AT BEGINNING OF PERIOD	847,235	7
CASH BALANCE AT END OF PERIOD	$ 339,068	$ 7
Supplemental Disclosures of Cash Flow Information:		
Interest Paid	$ -	$
Taxes Paid	$ 800	$
Schedule of noncash investing and financing activities:		
Issuance of common stock for:		
Notes Payable	$ 40,000	$
Accrued Interest	6,339	
	$ 46,339	$

NOTES TO INTERIM UNAUDITED FINANCIAL STATEMENTS

NOTE 1 - NATURE OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Business: Eye Dynamics, Inc. (the "Company') designs, develops, produces and markets diagnostic equipment that measures, tracks and records human eye movements, utilizing the Company's proprietary technology and computer software. The products perform separate, but related, functions and target two separate markets. First, the Company markets a neurological diagnostic product that tracks and measures eye movements during a series of standardized tests, as an aid in diagnosing problems of the vestibular (balance) system and other balance disorders. Second, the Company's impairment detection devices target the corporate and criminal justice markets and are designed to test individuals for impaired performance resulting from the influences of alcohol, drugs, illness, stress and other factors that affect eye and pupil performance. The Company is a Nevada corporation formed in 1989.

A summary of significant accounting policies follows:

Presentation of Interim Information: The financial information at June 30, 2005 and for the three and six months ended June 30, 2005 and 2004 is unaudited but includes all adjustments (consisting only of normal recurring adjustments) that the Company considers necessary for a fair presentation of the financial information set forth herein, in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") for interim financial information, and with the instructions to Form 10-QSB. Accordingly, such information does not include all of the information and footnotes required by U.S. GAAP for annual financial statements. For further information refer to the Consolidated Financial Statements and footnotes thereto included in the Company's Annual Report on Form 10-KSB for the year ended December 31, 2004.

The results for the three and six months ended June 30, 2005 may not be indicative of results for the year ending December 31, 2005 or any future periods.

Reclassification: Certain prior period balances have been reclassified to conform to the current period presentation.

NOTE 2 - BALANCE SHEET DETAILS

The following tables provide details of selected balance sheet items:

At June 30,	2005	2004
Property and equipment, net		
Furniture and Fixtures	$ 1,113	$ 1,113
Equipment	13,331	13,331
	14,444	14,444
Less: accumulated depreciation	(13,649)	(13,455)
Total	$ 795	$ 989

Other Assets		
Deferred tax assets	$ 217,957	$ 205,436
Deposits	1,563	13,662
Total	$ 219,520	$ 219,098
Accrued Liabilities		
Commission payable	$ 11,797	$ 10,770
Accrued insurance	6,831	-
Warranty reserve	7,458	6,779
Accrued interest	-	4,239
Other	431	(1,580)
Total	$ 26,517	$ 20,208

NOTE 3 - RETIREMENT OF DEBT

In April 2005, the Company converted notes payable of $40,000 and accrued interest of $6,339 into 3,591,799 shares of common stock pursuant to the conversion privileges stated in the original note agreements. As a result, the Company did not recognize any gain or loss from these conversions.

NOTE 4 - INCOME TAXES

The Company accounts for income taxes using a balance sheet approach whereby deferred tax assets and liabilities are determined based on the differences in financial reporting and income tax basis of assets and liabilities. The differences are measured using the income tax rate in effect during the year of measurement.

The Company experienced significant net losses in prior fiscal years resulting in a net operating loss carryforward ("NOLC") for federal income tax purposes of approximately $1.2 million at December 31, 2004. The Company's NOLC will expire through 2021. The Company also has state NOLC approximately of $530,000. The state NOLC will expire through 2013.

NOTE 5 - NET INCOME (LOSS) PER SHARE

The following table sets forth the computation of basic and diluted net income (loss) per share:

	Three Months ended June 30, 2005	2004	Six Mo 200
Basic net income (loss) per share:			
Net income (loss)	$ 39,579	$ 67,736	$ (35
Weighted average number of common shares	21,674,880	17,883,081	19,812
Basic net income (loss) per common share	$ 0.00	$ 0.00	$ (
Diluted net income (loss) per share:			
Net income (loss)	$ 39,579	$ 67,736	$ (35
Addback: Debenture interest	-	700	

Adjusted net income (loss)	$ 39,579	$ 68,436	$ (35
Weighted average number of common shares	21,674,880	17,883,081	19,812
Incremental shares from assumed conversion:			
Convertible debt	-	3,591,799	
Stock options and warrants	504,827	288,288	
Adjusted weighted average number of common shares	22,179,707	21,763,168	19,812
Diluted net income (loss) per common share	$ 0.00	$ 0.00	$ (

As the Company incurred net loss for the six months ended June 30, 2005, the effect of dilutive securities totaling 513,333 equivalent common shares have been excluded from the calculation of diluted net loss per share because their effect was anti-dilutive.

NOTE 6 - STOCK OPTIONS

On January 3, 2005, the Board of Directors approved to issue stock options to current directors for their services rendered in the amount of 20,000 shares for each of the years from 1999 through 2004, pursuant to approval granted in 1998 at the annual shareholders' meeting. The total options for each of directors shall be 120,000 shares. The options are vesting immediately and exercisable at $0.15 per share through January 3, 2007.

The Company accounts for these options under the recognition and measurement principles of APB Opinion No. 25, ACCOUNTING FOR STOCK ISSUED TO EMPLOYEES, AND RELATED INTERPRETATIONS. No stock-based employee compensation cost is reflected in net loss, as all options granted had an exercise price equal to the market value of the underlying common stock on the grant date. The following table illustrates the effect on net loss and net loss per share if the Company had applied the fair value provisions of FASB Statement No. 123, ACCOUNTING FOR STOCK-BASED COMPENSATION, to stock-based employee compensation.

	Three Months ended June 30, 2005	Six Months ended June 30, 2005
Net income (loss), as reported	$ 39,579	$ (35,881)
Deduct: Total stock-based employee compensation expense determined under the fair value of awards, net of tax related effects	-	39,600
Pro forma net income (loss)	$ 39,579	$ (75,481)
Reported net income (loss) per share-basic and diluted	$ 0.00	$ (0.00)
Pro forma net income (loss) per share-basic and diluted	$ 0.00	$ (0.01)

NOTE 7 - MAJOR CUSTOMERS

During the three and six months ended June 30, 2005, the private label distributor accounted for $362,197 and $616,950 or 89.92% and 85.72% of total revenues, respectively.

During the three months ended June 30, 2004, the private label distributor accounted for $327,659 or 71.8% of total revenues.

During the six months ended June 30, 2004, two customers accounted for $791,261 or 74.3% of total revenues.

Special Instrument Dealer 21.2%
Private label distributor 53.1%

NOTE 8 - SEGMENT INFORMATION

SFAS No. 131 "Disclosures about Segments of an Enterprise and Related Information" requires that a publicly traded company must disclose information about its operating segments when it presents a complete set of financial statements. Since the Company has only one segment; accordingly, detailed information of the reportable segment is not presented.

NOTE 9 - CHANGE OF OFFICERS

On January 11, 2005, the Board of Directors elected the Chairman of the Board to be the Company's new Chief Executive Officer (CEO). The former CEO remains as the Company's chief financial officer and president.

NOTE 10 - GUARANTEES AND PRODUCT WARRANTIES

The Company from time to time enters into certain types of contracts that contingently require the Company to indemnify parties against third party claims. These contracts primarily relate to: (i) divestiture agreements, under which the Company may provide customary indemnifications to purchasers of the Company's businesses or assets; (ii) certain real estate leases, under which the Company may be required to indemnify property owners for environmental and other liabilities, and other claims arising from the Company's use of the applicable premises; and (iii) certain agreements with the Company's officers, directors and employees, under which the Company may be required to indemnify such persons for liabilities arising out of their employment relationship.

The terms of such obligations vary. Generally, a maximum obligation is not explicitly stated. Because the obligated amounts of these types of agreements often are not explicitly stated, the overall maximum amount of the obligations cannot be reasonably estimated. Historically, the Company has not been obligated to make significant payments for these obligations, and no liabilities have been recorded for these obligations on its balance sheet as of June 30, 2005.

In general, the Company offers a one-year warranty for most of the products it sold. To date, the Company has not incurred any material costs associated with these warranties. The Company provides reserves for the estimated costs of product warranties based on its historical experience of known product failure rates, use of materials to repair or replace defective products and service delivery costs incurred in correcting product failures. In addition, from time to time, specific warranty accruals may be made if unforeseen technical problems arise with specific products. The Company periodically assesses the adequacy of its recorded warranty liabilities and adjusts the amounts as necessary.

The following table presents the changes in the Company's warranty reserve during the first six months of 2005:

Balance as of January 1, 2005	$ 8,884
Provision for warranty	1,748
Utilization of reserve	(3,174)
Balance as of June 30, 2005	$ 7,458

NOTE 11 - PENDING BUSINESS ACQUISITION

On March 24, 2005, the Company announced intent to acquire 100% issued and outstanding shares of OrthoNetx, Inc., a Colorado-based provider of medical devices for osteoplastic surgery. The acquisition will be completed as a stock transaction in which OrthoNetx shareholders will receive equal number of the Company's outstanding shares at the closing date. The acquisition is subject to certain customary conditions including certain regulatory approvals. As part of the transaction, the President and CEO of OrthoNetx will assume the position of CEO of the merged company.

NOTE 12 - SALES INCENTIVE AGREEMENTS

In April 2005, the Company entered into two individual agreements with the private label distributor and a special instrument dealer. The agreements provide that the Company will issue restricted common stock to the distributor and dealer as a sale incentive if certain conditions are reached pursuant to the agreements. As of June 30, 2005, none of these conditions are reached and the Company issued no shares.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

GENERAL

Certain of the statements contained in this report, including those under "Management's Discussion and Analysis or Plan of Operation," and especially those contained under "Liquidity and Capital Resources" may be "forward-looking statements" that involve risks and uncertainties. All forward-looking statements included in this report are based on information available to Eye Dynamics, Inc. ("the Company") on the date hereof and the Company assumes no obligation to update any such forward-looking statements. The actual future results of the Company could differ materially from those statements. Factors that could cause or contribute to such differences include, but are not limited to, those discussed in the Company's Annual Report on Form 10-KSB as well as risks associated with managing the Company's growth. While the Company believes that these statements are accurate, the Company's business is dependent upon general economic conditions and various conditions specific to the document and content management industry and future trends and results cannot be predicted with certainty.

RESULTS OF OPERATIONS (THREE MONTHS ENDED JUNE 30, 2005 COMPARED TO THREE MONTHS ENDED JUNE 30, 2004)

For the quarter ended June 30, 2005, the Company reported net income of

$39,579, or $0.00 per share, compared with net income of $67,736, or $0.00 per share for the corresponding quarter in 2004. The decrease is principally due to a decrease in revenues from $456,581 in 2004 to $402,785 in 2005. As cost of goods remained relatively constant as a percentage of revenues, and general and administrative expenses were relatively unchanged, the decrease in net income is almost entirely due to the reduction in revenues.

RESULTS OF OPERATIONS (SIX MONTHS ENDED JUNE 30, 2005 COMPARED TO SIX MONTHS ENDED JUNE 30, 2004)

For the six months ended June 30, 2005, the Company reported net loss of $35,881, or $0.00 per share, compared with net income of $208,101, or $0.01 per share, for the six months ended June 30, 2004. The loss in the current period is due primarily to an overall reduction in revenues from $1,065,347 in the 2004 period to 719,694 during the 2005 period, as well as an increase in general and administrative expenses from $348,153 to $415,355.

The increase in general and administrative expense is principally due to legal costs associated with the due diligence of the pending acquisition of OrthoNetx, as well as marketing costs associated with upcoming professional conventions and efforts to broaden our international sales program.

A reorganization of the Company's exclusive distributor (MedTrak Technologies, of Scottsdale, Arizona) that began in the first quarter of 2005 is beginning to show results. For instance, revenues for the second quarter of 2005 were 27% higher compared to the first quarter of 2005 ($316,909). As further evidence of the impact of the changes in the marketing organization and its strategies, July 2005 revenues were $161,576 (unaudited), and management believes this trend will continue. The company is working closely with the management of MedTrak to ensure that the marketing efforts related to the largest gathering of Ear, Nose and Throat specialists in the world - American Academy of Otolaryngology (in September of 2005) as well as the American Academy of Audiology (April of 2006)-- produce results in line with years past.

LIQUIDITY AND CAPITAL RESOURCES

Cash and cash equivalents as of June 30, 2005 of $739,068 allows for payment of all outstanding invoices on a current basis. Account payables are current and the Company has not borrowed against credit lines.

Inventory as of June 30, 2005 was $264,000, which is basically holding steady compared to that of the first quarter, even with the increase in sales.

Accounts receivable as of June 30, 2005 were higher then expected, at $158,232, because of an internal administrative error in an invoicing procedure. The error has been corrected and $99,049 of this amount was received in July. The company's aging amounts are a favorable representation of the company's generally excellent cash flow.

The company has placed a significant, yet appropriate, portion of its cash reserves into income producing products such as money market funds and date laddered certificates of deposit.

As announced on March 24, 2005, Eye Dynamics signed a Letter of Intent to acquire OrthoNetx, Inc., of Superior, Colorado. Both companies are continuing with their due diligence on the transaction, which has been proceeding in a satisfactory manner The transaction is subject to execution of a definitive Agreement and Plan of Merger, and is also subject to customary conditions, including regulatory approvals.

ITEM 3. CONTROLS AND PROCEDURES.

At the end of the period covered by this Form 10-QSB, the Company's management, including the Chief Executive and Chief Financial Officer, conducted an evaluation of the effectiveness of the Company's disclosure controls and procedures. Based on this evaluation, the Chief Executive and Chief Financial Officer have determined that such controls and procedures are effective to ensure that information relating to the Company required to be disclosed in reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission. There have been no changes in the Company's internal controls over financial reporting that were identified during the evaluation that occurred during the Company's last fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The Company is not a party to any pending legal proceedings.

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

During the period the Company issued 3,004,719 shares of Common Stock to three holders of Convertible Notes upon the conversion of the Convertible Notes. The Company believes these transactions were exempt from the registration provisions of the Securities Act of 1933 by reason of Section 4(2) thereof.

None

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

There were no matters submitted to the vote of security holders during this quarterly reporting period.

ITEM 5. OTHER INFORMATION

None

ITEM 6. EXHIBITS

31.1 Certificate of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certificate of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certificate of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

32.2 Certificate of Chief Financial Officer pursuant to Section 906 of the

Sarbanes-Oxley Act of 2002

SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: August 15, 2005

By: /s/ Ronald A. Waldorf

Ronald A. Waldorf, Chief Executive Officer