EYE DYNAMICS INC
Form 10QSB
November 07, 2003

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 September 30, 2003.

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 September 30, 2003 was 17,850,313.

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

PART I. FINANCIAL INFORMATION

ITEM 1. Financial Statements

ASSETS

Current Assets	
Cash	$ 543,581
Accounts receivable	229,116
Employee loans and advances, net of allowance for loan loss of $58,218	407
Prepaid expenses	5,247
Inventory	187,051
TOTAL CURRENT ASSETS	965,402
Property and equipment, net of accumulated depreciation of $13,239	1,205
Other assets	29,674

TOTAL ASSETS	$ 996,281
LIABILITIES AND STOCKHOLDERS' EQUITY	
Current Liabilities	
Accounts payable and accrued expenses	$ 106,707
Notes payable, current portion	23,761
TOTAL CURRENT LIABILITIES	130,468
Long-term debt and accrued interest	422,471
TOTAL LIABILITIES	552,939
Stockholders' Equity	
Common stock, $0.001 par value; 50,000,000 shares authorized; 17,850,313 shares issued and outstanding	17,850
Paid-in capital	3,497,101
Accumulated deficit	(3,071,609)
	443,342
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 996,281

See Notes to Interim Unaudited Consolidated Financial Statements

EYE DYNAMICS, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)

	For Three Months ended September 30,		For Nine ended Sept
	2003	2002	2003
Net Sales			
Products	$ 1,095,602	$ 518,508	$ 2,436,228
Service	5,500	--	5,500
	1,101,102	518,508	2,441,728
Cost of Sales			
Products	529,334	240,258	1,227,442
Service	800	--	800
	530,134	240,258	1,228,242

Gross profit	570,968	278,250	1,213,486
Selling, general and administrative expenses	188,541	173,873	530,603
Operating income	382,427	104,377	682,883
Other income(expenses)			
Interest and other income	155	1,485	687
Interest and other expenses	(802)	(3,284)	(17,000)
Total other income(expenses)	(647)	(1,799)	(16,313)
Net income before taxes and extraordinary item	381,780	102,578	666,570
Provision for income taxes	33,173	--	60,269
Net income before extraordinary item	348,607	102,578	606,301
Extraordinary item-gain on restructuring of debt, net of applicable income taxes of $0	--	--	--
Net income	$ 348,607	$ 102,578	$ 606,301
Net income per share-Basic:			
Net income before extraordinary item	$ 0.02	$ 0.01	$ 0.03
Extraordinary item, net	--	--	--
Net income	$ 0.02	$ 0.01	$ 0.03
Net income per share-Diluted:			
Net income before extraordinary item	$ 0.02	$ 0.00	$ 0.03
Extraordinary item, net	--	--	--
Net income	$ 0.02	$ 0.00	$ 0.03
Shares used in per share calculation-Basic	17,850,313	17,350,313	17,850,313
Shares used in per share calculation-Diluted	21,706,001	22,738,013	21,696,712

See Notes to Interim Unaudited Consolidated Financial Statements

EYE DYNAMICS, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

For Nine Months ended September 30,	2003	2002

Cash Flow From Operating Activities:		
Net income	$ 606,301	$ 77,927
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation	306	1,108
Noncash expenses	--	149,557
Extraordinary gain on debt restructuring	--	(26,479)
(Increase) in:		
Accounts receivable	(42,139)	(98,017)
Inventory	(31,884)	(3,996)
Prepaids and other assets	(19,962)	(19,713)
Increase (decrease) in:		
Accounts payable and accrued expenses	17,301	993
Contingent liabilities	(13,271)	(75,000)
Accrued interest	(74,602)	(12,757)
CASH FLOWS PROVIDED BY (USED IN) OPERATING ACTIVITIES	442,050	(6,377)
Cash Flow From Investing Activities:		
Purchase of property and equipment	(1,113)	--
Employee loans and advances	(407)	3,452
CASH FLOWS PROVIDED BY (USED IN)INVESTING ACTIVITIES	(1,520)	3,452
Cash Flow From Financing Activities:		
Advance from (repayments on) line of credit	--	(1,458)
Net proceeds from (repayments on) notes payable to shareholder	--	(15,000)
Net proceeds from (repayments on) other notes payable	(74,617)	39,750
CASH FLOWS PROVIDED BY (USED IN) FINANCING ACTIVITIES	(74,617)	23,292
NET INCREASE IN CASH	365,913	20,367
Cash balance at beginning of period	177,668	23,623
CASH BALANCE AT END OF PERIOD	$ 543,581	$ 43,990
Supplemental Disclosures of Cash Flow Information:		
Interest Paid	$ 78,889	$ 23,459
Taxes Paid	39,242	1,600
Supplemental Schedules of Noncash Investing and Financing Activities		
Issuing common stock for:		
Services	$ --	$ 9,000
Reduction of liability	--	10,000
Restructuring of debt	--	100,000

See Notes to Interim Unaudited Consolidated Financial Statements

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

NATURE OF BUSINESS: Eye Dynamics, Inc. and subsidiary (the "Company") markets and distributes diagnostic equipment that utilize the Company's proprietary technology and computer software to test individuals for impaired eye and pupil performance. The Company also markets a medical diagnostic product that tracks and measures eye movements during a series of standardized tests.

A summary of significant accounting policies follows:

PRESENTATION OF INTERIM INFORMATION: The financial information at September 30, 2003 and for the three and nine months ended September 30, 2003 and 2002 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, 2002.

The results for the three and nine months ended September 30, 2003 may not be indicative of results for the year ending December 31, 2003 or any future periods.

PRINCIPLES OF CONSOLIDATION AND PRESENTATION: The accompanying consolidated financial statements include the accounts of Eye Dynamics, Inc. and its wholly-owned subsidiary, Oculokinetics, Inc., after elimination of all material intercompany accounts and transactions. Certain prior period balances have been reclassified to conform to the current period presentation.

DEBT RESTRUCTURINGS: The Company accounts for debt restructurings that occurred in April 2002 in accordance with Statement of Financial Accounting Standards (SFAS) No. 15, "Accounting for Debtors and Creditors for Troubled Debt Restructurings." The statement requires that a debtor should (a) recognize a gain or loss by reducing the carrying amount of the debt by the fair value of the assets or equity interest transferred, and (b) account for the remainder of the restructuring as a modification of debt terms. When the terms of a debt are adjusted in a trouble-debt restructuring, the total amount of the future cash payments should be determined. If the carrying amount of debt is less than the aggregate future cash payments required by the new debt term, the debtor should amortize the difference over the life of the new debt as interest expense using the effective interest method. No gain or loss is recognized in the period of extinguishments. If the carrying amount of debt is greater than the aggregate future cash payments required by the new debt term, the debtor should reduce the carrying value of debt to an amount equal to the total future cash payments and recognize the reduction an extraordinary gain. No interest expense should be recorded.

NET INCOME PER SHARE: Basic earnings per share includes no dilution and is computed by dividing net income available to common stockholders by the weighted average number of common stock outstanding for the period. Diluted earnings per share is computed by dividing net income by the weighted average number of shares plus the dilutive effect of outstanding warrants and shares issuable under convertible debt, using the treasury stock method. Options and warrants that are antidilutive because their average exercise price exceeded the average market price of the Company's common stock for the period approximated 200,000 and 350,000 for the three and nine months ended September 30, 2003 and 2002, respectively.

NOTE 2 - WIND DOWN OF SUBSIDIARY

On September 15, 2003, the Board of Directors approved the winding down Oculokinetics, Inc., a wholly-owned subsidiary, which was inactive and had no assets or liabilities as of that date. Management believes that the wind down of the subsidiary has no material effect on the Company's financial position, results of operations and cash flows.

NOTE 3 - NET INCOME PER SHARE

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

	Three Months ended September 30, 2003	Three Months ended September 30, 2002	Nine Mon Septe 2003
Numerator:			
Net Income	$ 348,607	$ 102,578	$ 606,301
Denominator:			
Weighted average of common shares	17,850,313	17,350,313	17,850,313
Diluted effect of convertible debt and stock warrants	3,855,688	5,387,700	3,846,399
Diluted weighted average common shares outstanding	21,706,001	22,738,013	21,696,712
Basic net income per share	$ 0.02	$ 0.01	$ 0.03
Diluted net income per share	$ 0.02	$ 0.00	$ 0.03

The net income amount for nine months ended September 30, 2002 included an after-tax amount of $26,479, which relates primarily to an extraordinary gain from restructuring of debt. Excluding the effects of these transactions, the basic and diluted income per share would have been the same.

NOTE 4 - PRIOR PERIOD ADJUSTMENT

An understatement of 2002 reported Income Tax Payable of $12,699 was discovered during the second quarter of 2003. The Company charged this error to the current quarter's operations and did not restate the 2002 financial statements. Management believes that the adjustment did not have a material effect on the Company's financial position, results of operations and cash flows.

NOTE 5 - MAJOR CUSTOMER

During the three months ended September 30, 2003 and 2002, the Company's private label distributor accounted for $643,132 and $342,538, or 58.4% and 66.1%, of total revenues, respectively.

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During the nine months ended September 30, 2003 and 2002, the Company's private label distributor accounted for $1,376,347 and $712,838, or 56.4% and 68.0%, of total revenues, respectively.

NOTE 6 - LETTER AGREEMENT

On July 11, 2002, the Company entered into a letter agreement with HRL Laboratories, LLC (HRL) to develop a robust iris eye tracking algorithm and image capture plus DSP architecture. As consideration for HRL's research and development, the Company is to issue to HRL (1) 300,000 shares of the Company's restricted common stock as initial compensation for execution of the first phase of the research and development project at date of agreement; (2) 300,000 additional shares upon the demonstration of the iris tracking algorithm; and (3) up to 200,000 additional shares prorated by solution cost at a maximum of 1,000 shares per unit cost. The maximum number of shares to be issued to HRL is 800,000 shares.

The Company will own all intellectual property developed under the project and HRL will have a royalty-free license throughout the universe to use such intellectual property.

HRL will also be given a non-voting seat on the Company's Board of Directors, to be filled by an individual selected in HRL's sole discretion.

All 800,000 shares have been issued in 2002, and the total cost of $28,000 was charged to operations. Of these shares, 300,000 shares were issued during the third quarter of 2002, and $9,000 was allocated and charged to the third quarter.

NOTE 7 - SEGMENT INFORMATION

The Company is currently managed and operated as one business. The entire business is managed by a single management team that reports to the Company's President. The Company does not operate separate lines of business or separate business entities with respect to any of its product candidates. Accordingly, the Company does not prepare discrete financial information with respect to separate product areas or by location and dose not have separately reportable segments as defined by SFAS No. 131 "Disclosures about Segments of an Enterprise and Related Information".

NOTE 8 - GUARANTEES

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 September 30, 2003.

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.

ITEM 2. Management's Discussion and Analysis or Plan of Operation

THREE MONTHS AND NINE MONTHS ENDED SEPTEMBER 30, 2003 COMPARED TO THREE MONTHS AND NINE MONTHS ENDED SEPTEMBER 30, 2002

Revenues from the sale of medical products during the third quarter were $1,101,000, representing an increase of 211% over the third quarter of 2002. This is the fifth quarter in succession where the sales are a minimum of two times the quarter of the prior year and is a reflection of the steady growth of the company. The increase is largely due to the success of the private label sales program for the Company's Video ENG Systems. Sales of the Company's own branded ENG products also increased substantially in the quarter, and for the year to date. The private label portion of our business accounted for 58% of revenues for the quarter, as opposed to 66% of revenues during the same quarter of 2002, and reflects the increase in Eye Dynamics brand product sales. The market increase in the ENT segment of the medical market is not substantial, but the neurology and mobile diagnostic testing continues to be successful.

Gross profit for the quarter was 53%, a significant improvement over the 43% gross profit in the previous quarter, which reflected extraordinary selling expenses. The Company's goal is to maintain a gross profit of at least 50% for each quarter and year to date. The Company is making efforts to contain expenses and to reduce product costs in order to achieve the gross profit percent goal.

Primarily as a result of the sales increase of 211% for the quarter, a net income (before taxes) of $381,780 was achieved, compared to $102,578 in the third quarter of 2002. This represents improved profitability for the Company for five successive quarters. After-tax net income for the quarter was $348,607, which includes provision for income taxes of $33,173.

Year to date net profit after taxes of $606,301 compares to $77,927 for the same period of 2002. This improvement is principally attributable to the substantial increase in revenues during 2003.

The Company incurred California state income taxes because the California Franchise Tax Board placed a moratorium on the use of tax loss carryovers for the years 2002 and 2003. Therefore, even though the Company has substantial tax loss carryovers from prior years, it was unable to use these to offset state income taxes in 2002 and 2003. Federal tax loss carryovers are not affected and therefore, the Company is not required to accrue federal income taxes for 2003.

LIQUIDITY AND CAPITAL RESOURCES

Cash and cash equivalents as of September 30, 2003 of $543,581 allows for payment of all outstanding invoices and our single note payment on a current basis. Accounts payable are current and the Company has not borrowed against credit lines.

Inventory of $187,000 at September 30, 2003 includes $25,000 of SafetyScope Impairment Detection Device items, which are not currently being actively marketed, but are used as production samples and demonstrators for capital-raising activities related to that business. The inventory balance of $162,000 represents less than one month of consumption, and is relatively balanced in content.

Accounts receivable of $229,000 represents less than 20 days accounts receivable aging, which is favorable as the Company's private label customer generally makes payment within the net 15 days term of sale. Other customers are utilizing leasing and credit cards with more frequency, providing for very quick collection of receivables.

The Company continues to seek financing for the business plan to commercialize the SafetyScope product, which is an Impairment Detection Device. The plan requires substantial financial resources to fully implement the commercialization of the product. Discussions and explorations of strategic alliances are ongoing with the goal of securing the financing; however the Company has no arrangements or agreements as to any such financing.

The Company continues to search out and evaluate other products and alliances to enhance its product lines and to augment revenues. The search for new products is an ongoing project.

Sales prospects for the balance of 2003 are encouraging, as evidenced by October revenues in the order of $300,000, which is our monthly target.

Item 3. Controls and Procedures.

Under the supervision and with the participation of our Chief Executive and Financial Officer, we conducted an evaluation of our disclosure controls and procedures, as such term is defined under Rule 13a-14(c) promulgated under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), within 90 days of the filing date of this report. Based on this evaluation, our Chief Executive and Financial Officer concluded that the Company's disclosure controls and procedures are effective. Disclosure controls and procedures are designed to ensure that information required to be disclosed in reports under the Exchange Act are processed and reported within the time periods specified by law.

Since the date of the evaluation described above, there have been no significant changes in our internal controls or in other factors that could significantly affect these controls.

PART II OTHER INFORMATION

Item 1. Legal Proceedings

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

Item 2. Changes In Securities And Use Of Proceeds

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 and Reports on Form 8-K

(a) Exhibits

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

32 Certificate of Chief Executive and Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

(b) Reports on Form 8-K

None.

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: November 7, 2003

By: /s/ Charles E. Phillips

Charles E. Phillips, President