TRIMEDYNE INC
Form 10-Q
February 21, 2012

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

FORM 10-Q

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended December 31, 2011

or

[_] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ____________________ to _______________________

COMMISSION FILE NO. 0-10581

TRIMEDYNE, INC.

Exact Name of Registrant as Specified in its Charter)

| | |
|---|---|
| NEVADA<br>(STATE OR OTHER JURISDICTION<br>OF INCORPORATION) | 36-3094439<br>(I.R.S. EMPLOYER<br>IDENTIFICATION NO.) |
| 25901 COMMERCENTRE DRIVE<br>LAKE FOREST, CALIFORNIA<br>(ADDRESS OF PRINCIPAL EXECUTIVE<br>OFFICES) | 92630<br>(ZIP CODE) |

Registrant's Telephone Number, Including Area Code:

(949) 951-3800

Securities Registered Pursuant to Section 12(b) of the Act:
NONE

Securities Registered Pursuant to Section 12(g) of the Act:

Common Stock, $.01 Par Value per Share
(Title of Class)

Indicate by check mark whether the registrant (1) has filed all reports 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 (ss. 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes [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 | [_] | 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 of 1934). Yes [_] No [X]

As of February 17, 2012, there were outstanding 18,395,960 shares of registrant's Common Stock.

TRIMEDYNE, INC.

TRIMEDYNE, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(UNAUDITED)

ASSETS

| | December 31, 2011 | September 30, 2011 |
|---|---|---|
| Current assets: | | |
| Cash and cash equivalents | $706,000 | $1,151,000 |
| Trade accounts receivable, net of allowance for doubtful accounts of $11,000 at December 31, 2011 and September 30, 2011 | 504,000 | 598,000 |
| Inventories | 2,320,000 | 2,162,000 |
| Other current assets | 152,000 | 143,000 |
| Total current assets | 3,682,000 | 4,054,000 |
| | | |
| Property and equipment, net | 951,000 | 1,027,000 |
| Other | 84,000 | 92,000 |
| Goodwill | 544,000 | 544,000 |
| | | |
| Total Assets | $5,261,000 | $5,717,000 |
| | | |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| | | |
| Current liabilities: | | |
| Accounts payable | $211,000 | $270,000 |
| Accrued expenses | 444,000 | 428,000 |
| Deferred revenue | 74,000 | 93,000 |
| Accrued warranty | 25,000 | 38,000 |
| Current portion of note payable and capital leases | 78,000 | 133,000 |
| Note payable to related party | 156,000 | 187,000 |
| Accrued interest due to related party | -- | 1,000 |
| Total current liabilities | 988,000 | 1,150,000 |
| | | |
| Note payable and capital leases, net of current portion | 6,000 | 13,000 |
| Deferred rent | 86,000 | 100,000 |
| | | |
| Total liabilities | 1,080,000 | 1,263,000 |
| | | |
| Commitments and contingencies | | |
| | | |
| Stockholders' equity: | | |
| Preferred stock - $0.01 par value, 1,000,000 shares authorized, none issued and outstanding | -- | -- |
| Common stock - $0.01 par value, 30,000,000 shares authorized, 18,497,569 and 18,467,569 shares issued at December 31, 2011 and September 30, 2011, respectively, 18,395,960 and 18,365,960 shares outstanding at December 31, 2011 and September 30, 2010, respectively | 186,000 | 186,000 |

| | | |
|---|---|---|
| Additional paid-in capital | 51,280,000 | 51,268,000 |
| Accumulated deficit | (46,572,000 ) | (46,287,000 ) |
| | 4,894,000 | 5,167,000 |
| Treasury stock, at cost (101,609 shares) | (713,000 ) | (713,000 ) |
| Total stockholders' equity | 4,181,000 | 4,454,000 |
| Total liabilities and stockholder's equity | $5,261,000 | $5,717,000 |

See accompanying notes to condensed consolidated financial statements

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TRIMEDYNE, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

| | For the Three Months Ended December 31, | |
|---|---|---|
| | 2011 | 2010 |
| Net revenues | $1,390,000 | $1,635,000 |
| Cost of revenues | 870,000 | 1,026,000 |
| Gross profit | 520,000 | 609,000 |
| | | |
| Operating expenses: | | |
| Selling, general and administrative | 658,000 | 707,000 |
| Research and development | 210,000 | 210,000 |
| Total operating expenses | 868,000 | 917,000 |
| | | |
| (Loss) from operations | (348,000) | (308,000) |
| | | |
| Other income, net | 63,000 | 17,000 |
| | | |
| (Loss) before income taxes | (285,000) | (291,000) |
| | | |
| Provision for income taxes | -- | 2,000 |
| Net (loss) | $(285,000) | $(293,000) |
| | | |
| Net (loss) per share: | | |
| Basic | $(0.02) | $(0.02) |
| Diluted | $(0.02) | $(0.02) |
| | | |
| Weighted average number of shares outstanding: | | |
| Basic | 18,395,960 | 18,365,960 |
| Diluted | 18,395,960 | 18,365,960 |

See accompanying notes to condensed consolidated financial statements

TRIMEDYNE, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

| | Three Months Ended December 31, 2011 | 2010 |
|---|---|---|
| Cash flows from operating activities: | | |
| Net loss | $(285,000) | (293,000) |
| Adjustments to reconcile net loss to net cash used in operating activities: | | |
| Stock-based compensation | 12,000 | 4,000 |
| Depreciation and amortization | 76,000 | 63,000 |
| Amortization of debt discount | -- | 5,000 |
| Change in fair value of derivative liabilities | -- | (15,000) |
| Loss on disposal of fixed assets | -- | 2,000 |
| Changes in operating assets and liabilities: | | |
| Trade accounts receivable | 94,000 | (50,000) |
| Inventories | (158,000) | 142,000 |
| Other assets | (1,000) | (40,000) |
| Accounts payable | (59,000) | 71,000 |
| Accrued expenses | 16,000 | (2,000) |
| Accrued interest to related party | (1,000) | 8,000 |
| Income tax payable | -- | 2,000 |
| Deferred revenue | (19,000) | (14,000) |
| Accrued warranty | (13,000) | 6,000 |
| Deferred rent | (14,000) | 3,000 |
| Net cash used in operating activities | (352,000) | (108,000) |
| Cash flows from investing activities: | | |
| Purchase of property and equipment | -- | (12,000) |
| Net cash used in investing activities | -- | (12,000) |
| Cash flows from financing activities: | | |
| Principal payments on notes to related party | (31,000) | -- |
| Principal payments on notes payable and capital leases | (62,000) | (55,000) |
| Net cash used in financing activities | (93,000) | (55,000) |
| Net decrease in cash and cash equivalents | (445,000) | (175,000) |
| Cash and cash equivalents at beginning of period | 1,151,000 | 2,528,000 |
| Cash and cash equivalents at end of period | $706,000 | $2,353,000 |
| Supplemental disclosure of cash flow information: | | |

No cash was paid for income taxes during the three months ended December 31, 2011 and 2010. Cash paid for interest during the three months ended December 31, 2011 and 2010 was approximately $4,000 and $10,000, respectively.

TRIMEDYNE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2011
(UNAUDITED)

NOTE 1 - Summary of Significant Accounting Policies

Principles of Consolidation

The accompanying condensed consolidated financial statements include the accounts of Trimedyne, Inc., a Nevada corporation, its wholly owned subsidiary, Mobile Surgical Technologies, Inc. ("MST"), a Texas corporation, and its 90% owned inactive subsidiary, Cardiodyne, Inc. ("Cardiodyne"), a Nevada corporation, (collectively, the "Company"). All intercompany accounts and transactions have been eliminated in consolidation.

Management's Plans

The Company is currently pursuing market development efforts in growth markets in Pacific Rim countries, Latin America and Eastern Europe. We believe that by expanding healthcare infrastructure in these markets we will create a sustained demand for Holmium Lasers applied to Spinal Endoscopy, Laser Lithotripsy and Laser prostate ablation. Additionally, we expect the global trend toward single-use disposable laser delivery products will improve sales and profit margins as more hospitals convert from multi-use products, due to concerns for sterility and interests to reduce handling costs incurred in product sterilization and we are developing more single-use products.

Subsequent to the period ended December 31, 2011, we received 19 purchase orders for future delivery of Lasers during the current fiscal year. We are expecting to have a significant increase in the sales of Lasers and laser products during the current fiscal year ending September 30, 2012.

In addition, in January 2012, we received $200,000 from the sale of three patents to a third party (See Note 7 “Subsequent Events” contained in the Notes to the Consolidated Financial Statements) which will be used to fund operations.

We believe that existing cash flows will be sufficient to fund operations through December 31, 2012; however, we have incurred losses from operations for the past four years. Although management expects that we will be able to maintain or achieve sales growth in the next 12 months, there is no guarantee that the Company will be profitable. Thus, it is possible that additional working capital in the next 12 to 24 months may be required. If necessary, we will raise additional debt and/or equity capital, sell some of our assets, reduce our costs by eliminating certain personnel positions and reducing certain overhead costs in order to fund operations. There is no guarantee that our efforts to do so will be successful.

Unaudited Interim Financial Information

The accompanying unaudited condensed consolidated financial statements have been prepared by the Company in accordance with accounting principles generally accepted in the United States of America for interim financial information, and pursuant to the instructions to Form 10-Q promulgated by the Securities and Exchange Commission ("SEC"). Accordingly, they do not include all information and disclosures required by generally accepted accounting principles for complete financial statement presentation. In the opinion of management, the accompanying condensed consolidated financial statements contain all adjustments (consisting of only normal recurring adjustments) necessary to present fairly the Company's consolidated financial position as of December 31, 2011 and the results of its operations and its cash flows for the three months ended December 31, 2011 and 2010. Results for the three months ended December 31, 2011 are not necessarily indicative of the results to be expected for the year ending September 30, 2012.

While management believes that the disclosures presented are adequate to make the information not misleading, it is suggested that these condensed consolidated financial statements be read in conjunction with the condensed consolidated financial statements and the notes included in the Company's 2011 annual report on Form 10-K for the year ended September 30, 2011.

Stock-Based Compensation

The fair value of stock-based awards is calculated using the Black-Scholes option pricing model. The Black-Scholes model requires subjective assumptions regarding future stock price volatility and expected time to exercise, which greatly affect the calculated values. The expected term of options granted is derived from historical data on employee exercises and post-vesting employment termination behavior. The risk-free rate selected to value any particular grant is based on the U.S. Treasury rate that corresponds to the pricing term of the grant effective as of the date of the grant. The expected volatility is based on the Company's historical volatilities of its common stock. These factors could change in the future, affecting the determination of stock-based compensation expense in future periods. On October 10, 2011, the Board of Directors approved the exchange of 171,000 out-of-money, fully-vested stock options, to certain employees, for an equal number of stock options at the current market price on that date of $0.13 per option. As a result of the modification, the Company recorded an additional expense of $9,000.

As of December 31, 2011, there was approximately $23,000 of total unrecognized compensation cost, net of estimated expected forfeitures, related to employee and director stock option compensation arrangements. This unrecognized cost is expected to be recognized on a straight-line basis over the next three years.

The following table summarizes stock-based compensation expense related to employee and director stock options under Accounting Standards Codification ("ASC") No. 718 Stock Compensation for the three months ended December 31, 2011 and 2010, which was allocated as follows:

| | Three Months Ended | |
|---|---|---|
| | December 31, 2011 | December 31, 2010 |
| Stock-based compensation included in: | | |
| Cost of revenues | $1,000 | $1,000 |
| Research and development expenses | $1,000 | $1,000 |
| Selling, general, and administrative expenses | $10,000 | $2,000 |

NOTE 2 - Composition of Certain Balance Sheet Captions

Inventories, net of reserves, consist of the following:

| | December 31, 2011 | September 30, 2011 |
|---|---|---|
| Raw materials | $1,047,000 | $948,000 |
| Work-in-process | 431,000 | 255,000 |
| Finished goods | 842,000 | 959,000 |
| | $2,320,000 | $2,162,000 |

For the three months ended December 31, 2011 and 2010, the aggregate net realizable value of demonstration and evaluation lasers did not comprise a material amount in inventories.

Other current assets consist of the following:

| | December 31, 2011 | September 30, 2011 |
|---|---|---|
| Royalty receivable | $31,000 | $5,000 |
| Prepaid insurance | 64,000 | 76,000 |
| Prepaid income tax | 3,000 | 3,000 |
| Prepaid rent | 33,000 | 33,000 |
| Short-term deposits | 8,000 | 8,000 |
| Other | 13,000 | 18,000 |
| Total other current assets | $152,000 | $143,000 |

Property and equipment consist of the following:

| | December 31, 2011 | September 30, 2011 |
|---|---|---|
| Furniture and equipment | $3,762,000 | $3,762,000 |
| Leasehold improvements | 643,000 | 643,000 |
| Other | 248,000 | 248,000 |
| | 4,653,000 | 4,653,000 |
| Less accumulated depreciation and amortization | (3,702,000 ) | (3,626,000 ) |
| Total property and equipment | $951,000 | $1,027,000 |

Accrued expenses consist of the following:

| | December 31, 2011 | September 30, 2011 |
|---|---|---|
| Accrued vacation | $170,000 | $174,000 |
| Accrued salaries and wages | 114,000 | 54,000 |
| Accrued bonus | 7,000 | 32,000 |
| Sales and use tax | 61,000 | 70,000 |
| Accrued legal | 16,000 | 16,000 |
| Customer deposits | 6,000 | 3,000 |
| Accrued commissions | 36,000 | 58,000 |
| Accrued PEO Expense | 18,000 | -- |
| Accrued payroll taxes | -- | 4,000 |
| Other | 16,000 | 17,000 |
| Total accrued expenses | $444,000 | $428,000 |

NOTE 3 - Note Payable to Related Party, Notes Payable and Capital Leases

Secured Note Payable to Related Party

On March 3, 2011, the Company was loaned $250,000 by Marcia H. Yeik Irrevocable Living Trust (the "Trust"), Marcia H. Yeik trustee thereof, the daughter of Marvin Loeb, CEO and Chairman, and the wife of Glenn D. Yeik, President and a member of the Board of Directors of the Company. Evidenced by a Note Payable (the "Note") with a principal amount of $250,000 at an interest rate of 12% per annum, the Note required monthly payments through April 2, 2013. The proceeds from the Note were used to pay accounts payable due to a vendor in connection with the purchase of property and equipment for MST. The Note was subordinated to the security interest of the holder of the Company's Senior Note, and was payable in increments applied to the principal at $10,416 per month along with accrued interest on the remaining principal over the life of the Note.

On June 27, 2011, with the consent of the related party and approval by the Board of Directors, the interest rate of the Note was amended to 6% per annum and the Trust had the right to call the Note at any time and demand immediate payment of all unpaid principal and all accrued interest.

As of December 31, 2011, the principal balance of the Note was $156,000. The Note was subsequently paid in full with accrued interest on January 3, 2012.

Notes payable and capital leases consists of the following at December 31, 2011 and September 30, 2011:

| | December 31, 2011 | September 30, 2011 |
|---|---|---|
| Capital lease agreement in connection with the purchasing of equipment bearing an effective interest rate of 9.25% per annum. The lease requires monthly payments of $4,979 through January 2013. | 57,000 | 70,000 |
| Capital lease agreement in connection with the purchasing of equipment bearing an effective interest rate of 9.23% per annum. The lease requires monthly payments of $526 through February 2013. | 7,000 | 8,000 |
| Capital lease agreement in connection with the purchasing of equipment bearing an effective interest rate of 8.82% per annum. The lease requires monthly payments of $2,403 through March 2012. | 6,000 | 13,000 |
| Finance agreement issued in connection with the purchasing of insurance policies. The note bears interest at 3.98% per annum and require monthly principal and interest payments of $13,803 through January 2012. | 14,000 | 55,000 |
| | $84,000 | $146,000 |
| | | |
| Less: current portion | (78,000) | (133,000) |
| | $6,000 | $13,000 |

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NOTE 4 - Commitments and Contingencies

Litigation

We are subject to various claims and actions that arise in the ordinary course of business. The litigation process is inherently uncertain, and it is possible that the resolution of any future litigation may adversely affect us.

The Company is currently a co-defendant in one product liability lawsuit. The case, filed on behalf of Paula Tsakonas, plaintiff, in the Circuit Court of Cook County, Illinois on February 23, 2011, relates to injuries that occurred in connection to a medical procedure in which the Company's laser was used and names Spiros G. Stamelos, MD, Stamelos Bros., LTD., an Illinois Corporation, doing business as Advanced Orthopaedic Associates, Lakeshore Surgery Center, LLC, an Illinois corporation and Trimedyne, Inc. as defendants. The case is currently in litigation. The Company has insurance to cover product liability claims. This insurance provides the Company with $5,000,000 of coverage for each occurrence with a general aggregate of $5,000,000. Trimedyne's liability is limited to a maximum of $25,000 per occurrence unless the judgment against the Company exceeds the insurance coverage. In such case, Trimedyne would be liable for any liability in excess of $5,000,000. Management had recorded a loss contingency for this claim in the amount of $25,000 based on the deductible under the insurance policy, of which $16,000 remains as of December 31, 2011. Management is not accruing any additional provision for this claim, as it is not expected that this claim will exceed the limits of the insurance coverage.

Guarantees and Indemnities

The Company has made certain indemnities and guarantees, under which it may be required to make payments to a guaranteed or indemnified party. The Company indemnifies its directors, officers, employees and agents to the maximum extent permitted under the laws of the State of California. In connection with its facility leases, the Company has indemnified its users of lasers for certain claims arising from the use of the lasers. The duration of the guarantees and indemnities varies, and in many cases is indefinite. These guarantees and indemnities do not provide for any limitation of the maximum potential future payments the Company could be obligated to make. Historically, the Company has not been obligated to make any payments for these obligations and no liabilities have been recorded for these indemnities and guarantees in the accompanying condensed consolidated balance sheet.

Risks and Uncertainties

The Centers for Medicare and Medicaid Services (CMS), the agency of the U.S. Government that administers the Medicare Program, does not reimburse for thermal intradiscal procedures to treat spinal discs including the use of the Company's pulsed Holmium Lasers. Since most people suffering from a herniated or ruptured spinal disc are below Medicare age, we do not believe CMS's decision will have an adverse impact on our business.

NOTE 5 - Segment Information

The Company's segments consist of individual companies managed separately with each manager reporting to the Chief Executive Officer. Revenues, and operating or segment profit, are reflected net of inter-segment sales and profits. Segment profit is comprised of net sales less operating expenses. Other income and expense and income taxes are not allocated and reported by segment since they are excluded from the measure of segment performance reviewed by management.

Data with respect to these operating activities for the three months ended December 31, 2011 and 2010 are as follows:

| | For the Three Months Ended December 31, 2011 | | | For the Three Months Ended December 31, 2010 | | |
|---|---|---|---|---|---|---|
| | Products | Service and Rental | Total | Products | Service and Rental | Total |
| Revenue | $ 776,000 | $ 614,000 | $ 1,390,000 | $ 929,000 | $ 706,000 | $ 1,635,000 |
| Cost of sales | 491,000 | 379,000 | 870,000 | 611,000 | 415,000 | 1,026,000 |
| Gross profit | 285,000 | 235,000 | 520,000 | 318,000 | 291,000 | 609,000 |
| Expenses: | | | | | | |
| Selling, general and administrative | 488,000 | 170,000 | 658,000 | 529,000 | 178,000 | 707,000 |
| Research and development | 210,000 | -- | 210,000 | 210,000 | -- | 210,000 |
| Income (loss) from operations | $ (413,000 ) | $ 65,000 | (348,000 ) | $ (421,000 ) | $ 113,000 | (308,000 ) |
| Other: | | | | | | |
| Interest income | | | -- | | | 1,000 |
| Interest expense | | | (4,000 ) | | | (18,000 ) |
| Royalty income | | | 31,000 | | | 19,000 |
| Change in fair market value of derivative liabilities | | | -- | | | 15,000 |
| Other income | | | 36,000 | | | -- |
| Provision for income tax | | | -- | | | (2,000 ) |
| Net loss | | | $ (285,000 ) | | | $ (293,000 ) |

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Sales and gross profit to customers by similar products and services for the three months ended December 31, 2011 and 2010 were as follows:

| | For the Three Months Ended December 31, | |
|---|---|---|
| | 2011 | 2010 |
| By similar products and services: | | |
| Revenues: | | |
| Laser equipment and accessories | $102,000 | $256,000 |
| Delivery and disposable devices | 674,000 | 673,000 |
| Service and rental | 614,000 | 706,000 |
| Total | $1,390,000 | $1,635,000 |
| | | |
| Gross profit | | |
| Laser equipment and accessories | $(21,000) | $15,000 |
| Delivery and disposable devices | 306,000 | 303,000 |
| Service and rental | 235,000 | 291,000 |
| Total | $520,000 | $609,000 |

Sales in foreign countries for the three months ended December 31, 2011 and 2010 accounted for approximately 25% and 18%, respectively, of the Company's total sales. The breakdown by geographic region is as follows:

| | Three Months Ended December 31, | |
|---|---|---|
| | 2011 | 2010 |
| Asia | $127,000 | $276,000 |
| Europe | 89,000 | 40,000 |
| Latin America | 99,000 | 44,000 |
| Australia | 39,000 | 11,000 |
| Middle East | -- | 8,000 |
| Other | -- | -- |
| | $354,000 | $379,000 |

All long-lived assets were located in the United States during the three months ended December 31, 2011 and 2010 with the exception of one laser located in Canada. Total segment assets at December 31, 2011 and 2010 for the Products segment were $3,448,000 and $5,714,000, respectively, and for the Service and Rental segment were $1,791,000 and $1,547,000, respectively. The $2,666,000 difference between total segment assets for the product segment for the current year quarter as compared to the prior year quarter was primarily the result of $2,000,000 received from a competitor as a result of a settlement agreement during the prior year. Total segment assets differ from total assets on a consolidated basis as a result of unallocated corporate assets primarily comprised of immaterial amounts of property and equipment, etc.

NOTE 6. RELATED-PARTY TRANSACTIONS

On April 7, 2006, the Company entered into an agreement to employ Cardiomedics as a consultant to provide graphics arts services, since the Company had no employee with experience in the design and production of brochures and other marketing materials. Under this agreement, Cardiomedics provides the services of a graphics art specialist at a rate comparable to those presently prevailing in the market in the design and production of marketing materials. The Company incurred $1,000 in expense for the services provided under the agreement, which was recorded to marketing expense during each of the periods ended December 31, 2011 and 2010.

See Note 3 for discussion note payable to related parties.

NOTE 7. SUBSEQUENT EVENTS

See Note 3 for discussion regarding repayment of $156,000 in notes payable to a related party.

In January 2012, the Company entered into an agreement for the sale of certain patents held by the Company to a third party. Under the terms of the agreement the Company received $200,000 and we received a non-exclusive, royalty free license to the patents. In addition, the Company will receive 35% of all net (after legal fees) proceeds received by the third party, up to $6 million, less the initial $200,000 payment and 50% of net proceeds over $6 million, if any.

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

FORWARD-LOOKING STATEMENTS

This information should be read in conjunction with the condensed consolidated financial statements and notes thereto included in Item 1 of Part I of this Quarterly Report and the audited consolidated financial statements and notes thereto and Management's Discussion and Analysis of Financial Condition and Results of Operations for the year ended September 30, 2011, contained in our 2011 Annual Report on Form 10-K.

The statements contained in this Quarterly Report on Form 10-Q that are not historical facts may contain forward-looking statements that involve a number of known and unknown risks and uncertainties that could cause actual results to differ materially from those discussed or anticipated by management. Potential risks and uncertainties include, among other factors, general business conditions, government regulations governing medical device approvals and manufacturing practices, competitive market conditions, success of the Company's business strategy, delay of orders, changes in the mix of products sold, availability of suppliers, concentration of sales in markets and to certain customers, changes in manufacturing efficiencies, development and introduction of new products, fluctuations in margins, timing of significant orders, and other risks and uncertainties currently unknown to management. We do not undertake any duty to update forward-looking statements after the date they are made or to conform them to actual results or to changes in circumstances or expectations.

OVERVIEW

Trimedyne, Inc. (the "Company", "we", "our" or "us") is engaged in the development, manufacturing and marketing of 80 and 30 watt Holmium "cold" pulsed lasers ("Lasers") and a variety of disposable and reusable, fiber optic laser energy delivery devices ("Fibers", "Needles" and "Tips") for use in a broad array of medical applications.

Our Lasers, Fibers, Needles and Tips have been cleared for sale by the U.S. Food and Drug Administration for use in orthopedics, urology, ear, nose and throat surgery, gynecology, gastrointestinal surgery, general surgery and other medical specialties. Many of the medical procedures in which our Lasers, Fibers, Needles and Tips are used are being reimbursed by Medicare and many insurance companies and health plans.

Our 100% owned subsidiary, Mobile Surgical Technologies, Inc. ("MST"), is engaged in the rental of lasers, along with the services of a trained operator and, if requested, the provision of applicable Fibers, Needles or Tips, on a "fee per case" basis to hospitals, surgery centers, group practices and individual physicians in Texas and nearby areas.

The principal market for our Lasers and Side Firing Needles is presently in orthopedics to treat herniated (bulging) and ruptured lumbar, thoracic and cervical discs in the spine, two of the four major causes of lower back, neck and leg pain, typically on an outpatient basis. Our Lasers and Tips are also used in orthopedics to treat damage in joints, such as the knee, shoulder, elbow, hip, ankle and wrist, in outpatient, arthroscopic procedures.

The Company's Lasers and Fibers are also used in Urology to fragment stones in the Kidney, ureter or bladder. The Company's new VaporMAX(R) Side Firing Optical Fiber device is also used to vaporize a portion of the male prostate which is used with the Company’s lasers in the treatment of benign prostate hyperplasia or "BPH", commonly referred to as an "enlarged prostate."

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CRITICAL ACCOUNTING POLICIES

Revenue Recognition

We prepare our consolidated financial statements in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements require the use of 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 amount of revenues and expenses during the reporting period. Our management periodically evaluates the estimates and judgments made. Management bases its estimates and judgments on historical experience and on various factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates as a result of different assumptions or conditions.

The methods, estimates, and judgment we use in applying our most critical accounting policies have a significant impact on the results we report in our financial statements. The SEC has defined "critical accounting policies" as those accounting policies that are most important to the portrayal of our financial condition and results, and require us to make our most difficult and subjective judgments, often as a result of the need to make estimates of matters that are inherently uncertain. Based upon this definition, our most critical estimates relate to the fair value of warrant liabilities. We also have other key accounting estimates and policies, but we believe that these other policies either do not generally require us to make estimates and judgments that are as difficult or as subjective, or it is less likely that they would have a material impact on our reported results of operations for a given period. For additional information see Note 2, "Summary of Significant Accounting Policies" in the notes to our reviewed financial statements appearing elsewhere in this quarterly report and our annual audited financial statements appearing on Form 10-K. Although we believe that our estimates and assumptions are reasonable, they are based upon information presently available, and actual results may differ significantly from these estimates.

RESULTS OF OPERATIONS

Method of Presentation

The unaudited condensed consolidated financial statements include the accounts of Trimedyne, Inc., its wholly owned subsidiary Mobile Surgical Technologies, Inc. ("MST") and its 90% owned subsidiary, Cardiodyne.

Quarter ended December 31, 2011 compared to quarter ended December 31, 2010

During the quarter ended December 31, 2011, net revenues were $1,390,000 as compared to $1,635,000 for the same period of the previous year, a $245,000 or 15% decrease. Net sales from lasers and accessories decreased by $154,000 or 60.2% to $102,000 during the three months ended December 31, 2011 from $256,000 in the same period of the prior year. Net sales from delivery and disposable devices remained relatively unchanged at $674,000 in the current quarter from $673,000 in the same quarter of the prior year. Net sales from service and rental decreased by $92,000 or 13% to $614,000 from $706,000 for the same quarters.

Cost of sales during the quarter ended December 31, 2011 was 62.5% of net revenue as compared to 62.8% of net revenues for the prior year quarter. Gross profit from the sale of lasers and accessories was (21.2)% as compared to 5.9% of net revenues for the prior year three-month period. The decrease in gross profit from the sale of Lasers was primarily due to a volumizing difference due to a lower production of Lasers resulting from the 60.2% decrease in sales of same. Gross profit from the sale of delivery and disposable devices was 45.0% for the current three-month period and the same period for the prior year. Gross profit from revenue received from service and rentals was 38.3% in the current quarter, as compared to 41.2% for the prior three-month period. The reduction in gross profit for service and rentals was primarily due to a decrease in sales from MST.

Selling, general and administrative expenses decreased in the current quarter to $658,000 from $707,000 in the prior year quarter, an decrease of $49,000 or 6.9%. The decrease in selling, general and administrative expenses was primarily the result of decreases of $66,000 in legal expense and $5,000 in commissions expense, offset by increases of $8,000 in stock-based compensation, $5,000 in rent expense and $4,000 in bank charges.

Research and development expenditures of $210,000 for the quarter ended December 31, 2011, remained relatively the same as compared $210,000 for the quarter ended December 31, 2010.

Other income, net increased by $48,000 or 320% to $63,000 in the first quarter ended December 31, 2011 from $15,000 in the first quarter of the prior year, primarily due to a an insurance settlement of $35,000 and an increase of $12,000 in royalty income received from Lumenis. Other income during the quarter ended December 31, 2010 primarily consisted of $19,000 of royalty income and $15,000 resulting from the change in fair market value of derivative liabilities, offset by $18,000 in interest expense.

For the current quarter, the Company had a net loss of $285,000 or $0.02 per share, based on 18,395,960 basic weighted average number of common shares outstanding, as compared to net loss of $293,000, or $0.02 per share, based on 18,365,960 basic weighted average number of common shares outstanding in the same quarter of the previous year.

Liquidity and Capital

At December 31, 2011, the Company had working capital of $2,694,000 compared to $2,904,000 at the end of the fiscal year ended September 30, 2011. Cash decreased by $445,000 to $706,000 from $1,151,000 at the fiscal year ended September 30, 2010. During the three month period ended December 31, 2011, net cash used in operating activities was $352,000. Net cash used in financing activities during the same three month period was $93,000, which was the result of payments on debt incurred for the servicing of loans for equipment and certain insurance policies and principal payments on related party notes.

The Company is currently pursuing market development efforts in growth markets in Pacific Rim countries, Latin America and Eastern Europe. We believe that by expanding healthcare infrastructure in these markets we will create a sustained demand for Holmium Lasers applied to Spinal Endoscopy, Laser Lithotripsy and Laser prostate ablation. Additionally, we expect the global trend toward single-use disposable laser delivery products will improve sales and profit margins as more hospitals convert from multi-use products, due to concerns for sterility and interests to reduce handling costs incurred in product sterilization and we are developing more single-use products.

Subsequent to the period ended December 31, 2011, we received 19 purchase orders for future delivery of Lasers during the current fiscal year. We are expecting to have a significant increase in the sales of Lasers and laser products during the current fiscal year ending September 30, 2012.

In addition, in January 2012, we received $200,000 from the sale of three patents to a third party (See Note 7 “Subsequent Events” contained in the Notes to the Consolidated Financial Statements) which will be used to fund operations.

We believe that existing cash flows will be sufficient to fund operations through December 31, 2012; however, we have incurred losses from operations for the past four years. Although management expects that we will be able to maintain or achieve sales growth in the next 12 months, there is no guarantee that the Company will be profitable. Thus, it is possible that additional working capital in the next 12 to 24 months may be required. If necessary, we will raise additional debt and/or equity capital, sell some of our assets, reduce our costs by eliminating certain personnel positions and/or replace certain overhead costs in order to fund operations. There is no guarantee that our efforts to do so will be successful.

OFF BALANCE SHEET ARRANGEMENTS

None.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK. N/A

ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures. Our management has evaluated, under the supervision and with the participation of our chief executive officer and principal financial officer, the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report pursuant to Rule 13a-15(b) under the Securities Exchange Act of 1934 (the "Exchange Act"). Based on that evaluation, our chief executive officer and principal financial officer have concluded that, as of the end of the period covered by this report, our disclosure controls and procedures are effective in ensuring that information required to be disclosed in our Exchange Act reports is (1) recorded, processed, summarized and reported in a timely manner, and (2) accumulated and communicated to our management, including our chief executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control Over Financial Reporting. During the period covered by this report, there have been changes in our internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. These changes were the remediation of the material weaknesses identified in Part II, Item 9, of our Annual Report on Form 10-K for the fiscal year ended September 30, 2011.

PART II Other Information

Item 1. Legal Proceedings

None

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

None

Item 3. Defaults Upon Senior Securities

None

Item 4. [Removed and Reserved]

Item 5. Other Information

None

Item 6. Exhibits

(a) Exhibits

| | |
|---|---|
| 31.1 | Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 for Marvin P. Loeb |
| 31.2 | Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 for Jeffrey S. Rudner |
| 32.1 | Chief Executive Officer Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |
| 32.2 | Principal Financial Officer Certification 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 Schema |
| 101.CAL | XBRL Calculation Linkbase |
| 101.DEF | XBRL Definition Linkbase |
| 101.LAB | XBRL Label Linkbase |
| 101.PRE | XBRL Presentation Linkbase |

SIGNATURE PAGE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned hereunto duly authorized.

| | | |
|---|---|---|
| | TRIMEDYNE, INC. | |
| Date: February 21, 2012 | By: | s/ Marvin P. Loeb<br>Marvin P. Loeb<br>Chairman and Chief Executive Officer |
| | TRIMEDYNE, INC. | |
| Date: February 21, 2012 | By: | s/ Jeffrey S. Rudner<br>Jeffrey S. Rudner<br>Principal Financial Officer |