NATUS MEDICAL INC
Form 10-Q
November 05, 2010
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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 September 30, 2010

¨ **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: 000-33001

NATUS MEDICAL INCORPORATED

(Exact name of registrant as specified in its charter)

Delaware	**77-0154833**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

1501 Industrial Road, San Carlos, CA 94070

(Address of principal executive offices) (Zip Code)

(650) 802-0400

(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 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 (§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 ¨ 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 the 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 x
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

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

The number of issued and outstanding shares of the registrant s Common Stock, $0.001 par value, as of October 29, 2010 was 28,908,955.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

NATUS MEDICAL INCORPORATED AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS (unaudited)

(in thousands, except share amounts)

	September 30, 2010	December 31, 2009
ASSETS		
Current assets:		
Cash and cash equivalents	$ 42,567	$ 32,586
Short-term investments	982	965
Accounts receivable, net of allowance for doubtful accounts of $1,810 in 2010 and $1,515 in 2009	41,018	43,750
Inventories	26,298	22,408
Prepaid expenses and other current assets	4,977	4,213
Deferred income tax	4,370	4,248
Total current assets	120,212	108,170
Property and equipment, net	15,771	14,066
Intangible assets	65,850	70,144
Goodwill	91,907	92,258
Other assets	6,610	6,853
Total assets	$ 300,350	$ 291,491
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 9,971	$ 11,074
Current portion of long-term debt	194	178
Accrued liabilities	13,788	17,245
Deferred revenue	5,301	4,705
Total current liabilities	29,254	33,202
Long-term liabilities:		
Long-term debt	782	931
Other liabilities	7,672	7,186
Deferred income tax	6,499	7,016
Total liabilities	44,207	48,335
Stockholders equity:		
Common Stock, $0.001 par value, 120,000,000 shares authorized; shares issued and outstanding 28,839,998 in 2010 and 28,380,967 in 2009	256,994	250,374

Retained earnings	12,282	5,737
Accumulated other comprehensive loss	(13,133)	(12,955)
Total stockholders equity	256,143	243,156
Total liabilities and stockholders equity	$ 300,350	$ 291,491

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

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NATUS MEDICAL INCORPORATED AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (unaudited)

(in thousands, except per share amounts)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Revenue	$ 53,279	$ 44,251	$ 155,136	$ 114,871
Cost of revenue	21,831	17,450	62,955	44,869
Gross profit	31,448	26,801	92,181	70,002
Operating expenses:				
Marketing and selling	12,693	11,767	40,046	32,005
Research and development	4,820	4,175	15,188	11,839
General and administrative	8,074	5,688	26,782	16,462
Total operating expenses	25,587	21,630	82,016	60,306
Income from operations	5,861	5,171	10,165	9,696
Other income (expense), net	(175)	71	11	584
Income before provision for income tax	5,686	5,242	10,176	10,280
Provision for income tax	1,943	1,573	3,631	3,488
Net income	$ 3,743	$ 3,669	$ 6,545	$ 6,792
Earnings per share:				
Basic	$ 0.13	$ 0.13	$ 0.23	$ 0.25
Diluted	$ 0.13	$ 0.13	$ 0.22	$ 0.24
Weighted average shares used in the calculation of earnings per share:				
Basic	28,212	27,669	28,021	27,640
Diluted	29,261	28,668	29,170	28,343

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

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NATUS MEDICAL INCORPORATED AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)

(in thousands)

	Nine Months Ended September 30,	
	2010	2009
Operating activities:		
Net income	$ 6,545	$ 6,792
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	6,467	5,840
Accounts receivable reserves	112	1,403
Warranty reserves	180	815
Loss on disposal of property and equipment	72	
Share-based compensation	4,013	3,047
Excess tax benefits on the exercise of options	(574)	(31)
Impairment of intangible assets	300	
Changes in operating assets and liabilities:		
Accounts receivable	2,085	1,959
Inventories	(6,048)	(612)
Prepaid expenses and other assets	(891)	597
Accounts payable	(859)	1,418
Deferred income tax	475	(155)
Accrued liabilities and deferred revenue	(2,283)	(157)
Net cash provided by operating activities	9,594	20,916
Investing activities:		
Cash paid for business acquisitions and earnout obligations, net of cash acquired	(19)	(47,142)
Purchases of property and equipment	(2,553)	(1,884)
Capitalized software development costs	(215)	(637)
Purchases of marketable securities	(975)	(944)
Sales of marketable securities	975	
Net cash used in investing activities	(2,787)	(50,607)
Financing activities:		
Proceeds from stock option exercises and ESPP purchases	2,033	542
Excess tax benefits on the exercise of options	574	31
Payments on borrowings	(134)	(385)
Net cash provided by financing activities	2,473	188
Exchange rate effect on cash and cash equivalents	701	1,267
Net increase (decrease) in cash and cash equivalents	9,981	(28,236)
Cash and cash equivalents, beginning of period	32,586	56,915
Cash and cash equivalents, end of period	$ 42,567	$ 28,679

Supplemental disclosure of cash flow information:		
Cash paid for interest	$ 44	$ 131
Cash paid for income taxes	$ 4,111	$ 268
Non-cash investing activities:		
Acquisition-related earnout obligations included in accrued liabilities	$	$ 19

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

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NATUS MEDICAL INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

1 - Basis of Presentation

The accompanying interim condensed consolidated financial statements of Natus Medical Incorporated (Natus, we, us, or the Company) have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). Except as updated below, the accounting policies followed in the preparation of the interim condensed consolidated financial statements are consistent in all material respects with those presented in Note 1 to the consolidated financial statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2009.

Interim financial reports are prepared in accordance with the rules and regulations of the Securities and Exchange Commission; accordingly, they do not include all of the information and notes required by GAAP for annual financial statements. The interim financial information is unaudited, but reflects all normal adjustments that are, in the opinion of management, necessary for the fair presentation of our financial position, results of operations, and cash flows for the interim periods presented. Operating results for the three and nine months ended September 30, 2010 are not necessarily indicative of the results that may be expected for the year ending December 31, 2010. The accompanying condensed consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation.

Comprehensive Income

Comprehensive income is comprised of net income and gains or losses resulting from currency translations of foreign investments. The details of comprehensive income are as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Net income	$ 3,743	$ 3,669	$ 6,545	$ 6,792
Foreign currency translation adjustment	1,990	597	(178)	1,400
Comprehensive income	$ 5,733	$ 4,266	$ 6,367	$ 8,192

Stockholders Equity

The details of changes in stockholders equity are as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Balance, beginning of period	$ 248,906	$ 232,619	$ 243,156	$ 226,494
Net income	3,743	3,669	6,545	6,792
Proceeds from stock option exercises and ESPP	26	129	2,033	542
Share-based compensation expense	1,683	1,273	4,013	3,047
Tax effect of option exercises	(205)	19	574	31
Foreign currency translation adjustment	1,990	597	(178)	1,400
Balance, end of period	$ 256,143	$ 238,306	$ 256,143	$ 238,306

Revenue Recognition

Revenue, net of discounts, is recognized from sales of medical devices and supplies, including sales to distributors, when the following conditions have been met: a purchase order has been received, title has transferred, the selling price is fixed or determinable, and collection of the resulting receivable is reasonably assured. Terms of sale for most domestic sales are FOB origin, reflecting that title and risk of loss are assumed by the purchaser at the shipping point; however, terms of sale for some neurology, sleep-diagnostic, and head cooling systems are FOB destination, reflecting that title and risk of loss are assumed by the purchaser upon delivery. Terms of sales to international distributors are EXW, reflecting that goods are shipped ex works, in which title and risk of loss are assumed by the distributor at the shipping point.

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NATUS MEDICAL INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited) (Continued)

We have historically applied the software revenue recognition rules as prescribed by Accounting Standards Codification (ASC) Subtopic 985-605 to sales of certain of our diagnostic neurology and hearing systems (products containing embedded software). In October 2009, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. (ASU) 2009-14, *Certain Revenue Arrangements That Include Software Elements*, which amended ASC Subtopic 985-605, and we adopted the provisions of ASU 2009-14 on January 1, 2010. This ASU removes tangible products containing software components and non-software components that function together to deliver the product s essential functionality from the scope of the software revenue recognition rules. In the case of the Company s products containing embedded software, we have determined that the hardware and software components function together to deliver the products essential functionality, and therefore, the revenue from the sale of these products no longer falls within the scope of the software revenue recognition rules. Our revenue recognition policies for sales of these products are now substantially the same as for our other tangible products.

Revenue from sales of certain of our products that remain within the scope of the software revenue recognition rules under ASC Subtopic 985-605 is not significant.

We previously accounted for arrangements with multiple deliverables under ASC Topic 605, where revenue was allocated to the deliverables based on vendor specific objective evidence (VSOE). In October 2009 the FASB issued ASU 2009-13, *Multiple Deliverable Revenue Arrangements*, which amends ASC Topic 605, and we adopted the provisions of ASU 2009-13 on January 1, 2010. Under the revenue recognition rules for tangible products as amended by ASU 2009-13, we now allocate revenue from arrangements with multiple deliverables to each of the deliverables based upon their relative selling prices as determined by a selling-price hierarchy. A deliverable in an arrangement qualifies as a separate unit of accounting if the delivered item has value to the customer on a stand-alone basis. The principal deliverables in our multiple deliverable arrangements that qualify as separate units of accounting consist of (i) sales of medical devices and supplies, (ii) installation services, (iii) extended service and maintenance agreements, and (iv) upgrades to embedded software.

The new rules establish a hierarchy to determine the selling price to be used for allocating revenue to deliverables as follows: (i) vendor-specific objective evidence of fair value (VSOE), (ii) third-party evidence of selling price (TPE), and (iii) best estimate of the selling price (ESP). VSOE of fair value is defined as the price charged when the same element is sold separately, or if the element has not yet been sold separately, the price for the element established by management having the relevant authority when it is probable that the price will not change before the introduction of the element into the marketplace. VSOE generally exists only when we sell the deliverable separately and is the price actually charged for that deliverable. We have previously established VSOE for substantially all of the deliverables in our multiple element arrangements; however, in the future we may rely on ESPs, reflecting our best estimates of what the selling prices of elements would be if they were sold regularly on a stand-alone basis, to establish the amount of revenue to allocate to the deliverable. TPE generally does not exist for our products because of their uniqueness.

For products shipped under FOB origin or EXW terms, delivery is generally considered to have occurred when shipped. Undelivered elements in our sales arrangements, which are not considered to be essential to the functionality of a product, generally include installation or training services that are performed after the related products have been delivered. Revenue related to undelivered installation services is deferred until such time as installation is complete at the customer s site. Revenue related to training services is recognized when the service is provided. Fair value for installation or training services is based on the price charged when the service is sold separately. The fair value of installation and training services is based upon billable hourly rates and the estimated time to complete the service.

Revenue from extended service and maintenance agreements, for both medical devices and data management systems, is recognized ratably over the service period. Freight charges billed to customers are included in revenue and freight-related expenses are charged to cost of revenue. Advance payments from customers are recorded as deferred revenue and recognized as revenue as otherwise described above. We generally do not provide rights of return on products. We accept trade-ins of our own and competitive medical devices. Trade-ins are recorded as a reduction of the replacement medical device sale. Provisions are made for initial standard warranty obligations that are generally one year in length.

More than 90% of the hospitals in the U.S. are members of Group Purchasing Organizations (GPO s), which negotiate volume purchase prices for member hospitals, group practices, and other clinics. Our agreements with GPOs typically contain preferential terms for the GPO and its members, including provisions for some, if not all, of the following:

Negotiated pricing for all group members;

Volume discounts and other preferential terms on their member s direct purchases from us;

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NATUS MEDICAL INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited) (Continued)

Promotion of Natus products by the GPO to its members;

Payment of marketing fees by Natus to the GPO, usually based on purchasing experience of group members; and

Non-recourse cancellation provisions.

We do not sell products to GPOs. Hospitals, group practices and other clinics that are members of a GPO purchase products directly from the Company under the terms negotiated by the GPO. Negotiated pricing and discounts are recognized as a reduction of the selling price of products at the time of the sale. Revenue from sales to members of GPOs is otherwise consistent with general revenue recognition policies as previously described.

Other than the increased disclosure requirements of adoption of ASU 2009-13 and ASU 2009-14, the adoption of these provisions did not change our units of accounting, allocation of arrangement consideration, or pattern or timing of revenue recognition. It also did not have a significant impact on our financial position, results of operations, or cash flows for the nine months ended September 30, 2010, nor do we anticipate a significant impact for the year ended December 31, 2010.

Recent Accounting Pronouncements

In January 2010, the FASB issued ASU 2010-06, *Improving Disclosures about Fair Value Measurements* (Topic 820): *Fair Value Measurement*. ASU 2010-06 requires new disclosures on the amount of and reason for transfers in and out of Level 1 and 2 fair value measurements, disclosure of activities, including purchases, sales, issuances, and settlements within Level 3 fair value measurements, and clarifies existing disclosure requirements on levels of disaggregation and disclosures about inputs and valuation techniques. The Company adopted ASU 2010-06 on January 1, 2010. The adoption of ASU 2010-06 did not impact our financial position, results of operations, cash flows, and associated disclosures.

In October 2009, the FASB issued ASU 2009-13, *Revenue Recognition* (Topic 605): *Multiple Deliverable Revenue Arrangements*, which amends ASC 605-25, *Revenue Recognition - Multiple-Element Arrangements*. ASU 2009-13 replaces the concept of allocating revenue consideration among deliverables in a multi-element revenue arrangement according to fair value with an allocation based on selling price. ASU 2009-13 also establishes a hierarchy for determining the selling price of revenue deliverables sold in multiple element revenue arrangements. The selling price used for each deliverable will be based on vendor-specific objective evidence (VSOE) if available, third-party evidence if VSOE is not available, or management s estimate of an element s stand-alone selling price if neither VSOE nor third-party evidence is available. The amendments in this update also require that an allocation of selling price among deliverables be performed based upon each deliverable s relative selling price to total revenue consideration, rather than on the residual method previously permitted. ASU 2009-13 is effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. Early adoption is permitted, but then requires retrospective application of its provisions from the beginning of the fiscal year. As noted above we adopted ASU 2009-13 on January 1, 2010.

In October 2009, the FASB issued ASU 2009-14, *Certain Revenue Arrangements That Include Software Elements,* which amends ASC 985-605, *Revenue Recognition - Software*. ASU 2009-14 changes the accounting model in revenue arrangements for products that include both tangible and software elements. Tangible products containing software components and non-software components that function together to deliver the tangible product s essential functionality are no longer within the scope of the software revenue guidance in ASC 985-605. ASU 2009-14 is effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. Early adoption is permitted, but then requires retrospective application of its provisions from the beginning of the fiscal year. As noted above, we adopted ASU 2009-14 on January 1, 2010

In February 2009, Accounting Standards Codification (ASC) 805-20-35-3, *Accounting for Assets Acquired and Liabilities Assumed in a Business Combination That Arise from Contingencies*, was revised. The revisions relate to the initial recognition and measurement, subsequent measurement, and disclosure of assets and liabilities arising from contingencies in a business combination under ASC Topic 805. We adopted the provisions of ASC 805-20-35-3 on September 1, 2009. See Note 2.

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NATUS MEDICAL INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited) (Continued)

2 - Business Combinations, Goodwill, and Intangible Assets

Alpine Biomed Holdings Corp.

We acquired Alpine Biomed Holdings Corp. (Alpine Biomed) on September 14, 2009 for $43.2 million in cash pursuant to an Agreement and Plan of Merger. The Agreement and Plan of Merger also included an earnout provision based on the achievement of a certain revenue target as of December 31, 2009, however, the revenue target was not achieved and no additional cash consideration has been paid.

We recorded adjustments to the original estimate of the purchase price allocation of the fair value of the assets acquired and liabilities assumed that decreased the carrying amount of goodwill by $112,000 and $34,000, respectively, for the three and nine months ended September 30, 2010, due to adjustments to inventories, intangible assets, accounts payable, deferred taxes, and accrued expenses.

Goodwill

The carrying amount of goodwill and the changes in those balances are as follows (in thousands):

Balance, January 1, 2010	$ 92,258
Purchase accounting adjustments	(34)
Adjustments associated with earnout provisions	22
Foreign currency translation	(339)
Balance, September 30, 2010	$ 91,907

Amortization of Intangible Assets with Finite Lives Acquired Through Business Combinations

Amortization of intangible assets associated with our business combinations was $1.2 million and $3.6 million for the three and nine months ended September 30, 2010, respectively, and $1.0 million and $3.1 million for the three and nine months ended September 30, 2009, respectively.

Impairment of Intangible Assets with Indefinite Lives

During the nine months ended September 30, 2010 we recorded an impairment charge of $300,000 to write down the entire carrying value of tradenames associated with the Sonamed Clarity product line. The write-down was the result of our decision to discontinue the Sonamed Clarity product line and to convert customers to other Natus newborn hearing screening products.

Capitalized Software Development Costs

Pursuant to ASC 350-40, we capitalized software development costs of $54,000 and $215,000 during the three and nine months ended September 30, 2010, respectively, and $293,000 and $637,000 during the three and nine months ended September 30, 2009, respectively.

We report capitalized software development costs as a component of intangible assets. Amortization of capitalized software development costs was $147,000 and $441,000 during the three and nine months ended September 30, 2010, respectively, and $50,000 and $235,000 during the three and nine months ended September 30, 2009, respectively.

3 - Basic and Diluted Earnings Per Common Share

Earnings per share is computed in accordance with ASC 260-10. Basic earnings per share is based upon the weighted average number of common shares outstanding during the period. Diluted earnings per share is based upon the weighted average number of common shares outstanding and dilutive common stock equivalents outstanding during the period. Common stock equivalents are options granted and shares of restricted stock issued under our stock awards plans and are calculated under the treasury stock method. Common equivalent shares from unexercised stock options and restricted stock are excluded from the computation when there is a loss as their effect is anti-dilutive, or if the exercise price of such options is greater than the average market price of the stock for the period.

For the three and nine months ended September 30, 2010, common stock equivalents of 1,049,368 and 1,148,698 shares, respectively, were included in the weighted average shares outstanding used to calculate diluted earnings per share. For the three and nine months ended September 30, 2010, common stock equivalents of 1,387,463 and 999,899 were excluded from the calculation of diluted earnings per share because the exercise price of such options was greater than the average market price of the stock for the periods. For the three and nine months ended September 30, 2009, common stock equivalents of 998,969 and 702,751 shares, respectively, were included in the weighted average shares outstanding used to calculate diluted earnings per share. For the three and nine months ended September 30, 2009, common stock equivalents of 1,411,152 and 1,594,888 shares, respectively, were excluded from the calculation of diluted earnings per share because of their anti-dilutive effect.

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NATUS MEDICAL INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited) (Continued)

4 - Inventories

Inventories consist of the following (in thousands):

	September 30, 2010	December 31, 2009
Raw materials and subassemblies	$ 11,361	$ 11,506
Finished goods	19,372	14,994
Total Inventories	30,733	26,500
Less: Non-current inventories	(4,435)	(4,092)
Inventories, net	$ 26,298	$ 22,408

Non-current inventories consist primarily of service components used to repair products held by our customers pursuant to warranty obligations and extended service agreements, including service components for products we are not currently selling. Management believes that these inventories will be utilized for their intended purpose.

Work in process represents an immaterial amount in all periods presented.

5 - Property and Equipment

Property and equipment consist of the following (in thousands):

	September 30, 2010	December 31, 2009
Land	$ 3,403	$ 3,403
Buildings	4,691	4,691
Leasehold improvements	1,981	1,479
Office furniture and equipment	8,012	7,898
Computer software and hardware	5,920	5,091
Demonstration and loaned equipment	8,717	6,286
	32,724	28,848
Accumulated depreciation	(16,953)	(14,782)
Total	$ 15,771	$ 14,066

Depreciation and amortization expense of property and equipment was $850,000 and $2.4 million for the three and nine months ended September 30, 2010, respectively, and was $313,000 and $2.4 million for the three and nine months ended September 30, 2009, respectively.

6 - Reserve for Product Warranties

We provide a warranty on all medical device products that is generally one year in length. We also sell extended service agreements on our medical device products. Service for domestic customers is provided by Company-owned service centers that perform all service, repair and calibration services. Service for international customers is provided by a combination of Company-owned facilities and third-party vendors on a contract basis.

We have accrued a warranty reserve, included in accrued liabilities on the accompanying balance sheets, for the expected future costs of servicing products during the initial warranty period. We base the liability on actual warranty costs incurred to service those products. On new products, additions to the reserve are based on a combination of factors including the percentage of service department labor applied to warranty repairs, as well as actual service department costs, and other judgments, such as the degree to which the product incorporates new technology. The reserve is reduced as costs are incurred to honor existing warranty obligations or when current facts indicate that the original estimates of expected future costs of servicing products were overstated.

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NATUS MEDICAL INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited) (Continued)

The details of activity in the warranty reserve are as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Balance, beginning of period	$ 563	$ 1,028	$ 694	$ 1,076
Warranty assumed through acquisitions		520		520
Warranty accrued for the period	94	176	180	815
Repairs for the period	(86)	(99)	(303)	(786)
Balance, end of period	$ 571	$ 1,625	$ 571	$ 1,625

The estimates we use in projecting future product warranty costs may prove to be incorrect. Any future determination that our product warranty reserves are understated could result in increases to our cost of sales and reductions in our operating profits and results of operations.

7 - Share-Based Compensation

At September 30, 2010, we have the following plans that give rise to share-based compensation: (i) two active stock option plans, the Amended and Restated 2000 Stock Awards Plan and the 2000 Director Option Plan, and (ii) the 2000 Employee Stock Purchase Plan. The terms of awards granted during the nine months ended September 30, 2010 and our methods for determining grant-date fair value of the awards were consistent with those described in the consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2009.

Detail of share-based compensation expense is as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Cost of revenue	$ 41	$ 117	$ 111	$ 208
Marketing and sales	493	326	1,096	739
Research and development	90	87	296	159
General and administrative	1,059	743	2,510	1,941
Total	$ 1,683	$ 1,273	$ 4,013	$ 3,047

As of September 30, 2010, unrecognized compensation expense related to the unvested portion of our stock options and other stock awards was approximately $13.7 million, which is expected to be recognized over a weighted average period of 2.8 years.

Stock Options

Activity in our stock option plans during the nine months ended September 30, 2010 is as follows:

	Shares	Weighted Average Exercise Price	Weighted-Average Remaining Contractual Life (Years)	Aggregate Intrinsic Value ($ 000 s)
Outstanding, beginning of period	3,435,394	$ 9.99		
Granted	467,700	$ 16.60		
Exercised	(215,054)	$ 7.33		
Cancelled	(38,612)	$ 14.84		
Outstanding, end of period	3,649,428	$ 10.95	3.81	$ 16,815
Exercisable, end of period	2,593,546	$ 9.46	3.39	$ 15,073
Vested and expected to vest, end of period	3,470,471	$ 10.76	3.74	$ 16,524

The intrinsic value of options exercised during the nine months ended September 30, 2010 was $1.6 million.

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NATUS MEDICAL INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited) (Continued)

Restricted Stock Awards

Activity in our stock plans related to restricted stock awards during the nine months ended September 30, 2010 is as follows:

	Shares	Weighted-Average Grant Date Fair Value	Remaining Cost Expected To Be Recognized ($ 000 s)
Unvested, beginning of period	547,784	$ 13.87	
Granted	208,900	$ 16.73	
Vested	(157,834)	$ 16.10	
Forfeited		$	
Unvested, end of period	598,850	$ 14.28	$ 8,294

We award restricted stock awards to U.S. employees of the Company that vest 50% upon the second anniversary of the vesting start date and 25% upon each of the third and fourth anniversaries of the vesting start date. We also award restricted stock awards to non-employee directors of the Company that vest on the first anniversary of the grant date.

Restricted Stock Units

Activity in our stock plans related to the award of restricted stock units during the nine months ended September 30, 2010 is as follows:

	Shares	Weighted-Average Remaining Contractual Life (Years)	Aggregate Intrinsic Value ($ 000 s)
Outstanding, beginning of period	66,500		
Awarded	32,450		
Released	(6,500)		
Forfeited	(18,900)		
Outstanding, end of period	73,550	1.93	$ 1,080

We award restricted stock units to non-U.S. employees of the Company that vest 50% upon the second anniversary of the vesting start date and 25% upon each of the third and fourth anniversaries of the vesting start date.

8 - Other income (expense), net

Other income (expense), net consisted of (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Investment income	$ 34	$ 40	$ 30	$ 218
Interest expense	(13)	(18)	(49)	(131)
Foreign currency exchange gain (loss)	(280)	183	(647)	159
Other income (expense)	84	(134)	677	338
Total other income (expense), net	$ (175)	$ 71	$ 11	$ 584

9 - Income Taxes

Provision for Income Tax

We recorded a provision for income tax of $1.9 million and $3.6 million for the three and nine months ended September 30, 2010, respectively. Our effective tax rate was 34.2% and 35.7% for the three and nine months ended September 30, 2010, respectively.

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NATUS MEDICAL INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited) (Continued)

We recorded a provision for income tax of $1.6 million and $3.5 million for the three and nine months ended September 30, 2009, respectively. Our effective tax rate was 30.0% and 33.9% for the three and nine months ended September 30, 2009, respectively.

Deferred Income Taxes

We account for income taxes in accordance with ASC 740-10, which requires that deferred tax assets and liabilities be recognized using enacted tax rates for the effect of temporary differences between the book and tax bases of recorded assets and liabilities. ASC 740-10 also requires that deferred tax assets be reduced by a valuation allowance if it is more likely than not that some or all of the deferred tax assets will not be realized. We have provided a valuation allowance on certain deferred tax assets in foreign locations where we believe it is more likely than not that those deferred tax assets would be recognized.

Uncertain Tax Positions

We have cumulatively accrued approximately $881,000 for estimated interest and penalties related to uncertain tax positions at September 30, 2010. We recorded approximately $76,000 and $234,000 of interest and penalties related to unrecognized tax positions as a component of income tax expense during the three and nine months ended September 30, 2010 and approximately $51,000 and $153,000 of interest and penalties related to unrecognized tax positions as a component of income tax expense during the three and nine months ended September 30, 2009, respectively.

Our tax returns remain open to examination as follows: U.S. federal, 2005 through 2009; U.S. states, generally 2004 through 2009; significant foreign jurisdictions, generally 2006 through 2009.

10 - Restructuring Reserve

On January 13, 2010, we adopted a reorganization plan (the Restructuring Plan) that is designed to eliminate redundant costs resulting from our acquisition of Alpine Biomed and to improve efficiencies in operations. Under the plan, Alpine operations in Montreal, Canada will be transitioned to our existing Xltek facility in Oakville, Ontario, Canada, and Alpine s sales organization will be merged into our global sales organization. These activities were substantially completed during the first and second quarters of 2010.

The Restructuring Plan will result in a staff reduction of approximately 70 employees for which we recorded a restructuring charge for severance benefits of approximately $3.0 million during the first fiscal quarter of 2010, which was reduced by $268,000 during the second fiscal quarter. In addition, during the second fiscal quarter of 2010 we recorded a $300,000 charge for a lease termination fee. We also recorded a $44,000 charge to write off property and equipment.

We account for restructuring costs in accordance with ASC Topic 420, *Exit or Disposal Cost Obligations*. The balance of the reserve is included in accrued liabilities on the accompanying balance sheets. Substantially all of the costs associated with the Restructuring Plan will result in cash expenditures.

Detail of activity in the restructuring reserve is as follows, (in thousands):

	Balance January 1, 2010	Charged To Expense	Accrual Reversal	Amounts Paid	Balance September 30, 2010
Employee termination benefits	$	$ 3,030	$ (268)	$ (2,636)	$ 126
Lease termination fee		300		(300)	

Totals	$	$ 3,330	$ (268)	$ (2,936)	$ 126

In addition to the above charges, the Company will incur other costs directly associated with the Restructuring Plan that do not qualify for accrual and reporting under ASC Topic 420 and are charged to expense as incurred. The Company charged to expense approximately $131,000 of such costs during the nine months ended September 30, 2010.

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NATUS MEDICAL INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited) (Continued)

11 - Debt and Credit Arrangements

Long-term borrowings are comprised of the following (2010 and 2009 columns in thousands):

	September 30, 2010	December 31, 2009
Term loan $2.9 million Canadian (CAD), interest at cost of funds plus 2.5%, due September 15, 2014 with principle repayable in monthly installments of $16,000 until August 15, 2014 and one final payment of $404,000 collateralized by a first lien on land and building owned by Xltek	$ 944	$ 1,062
Term loan CAD $300,000, interest at cost of funds plus 2.5% due November 15, 2010 with principle repayable in monthly installments of $2,000 until October 10, 2010 and one final payment of $36,000 collateralized by various assets of Xltek	32	47
Total long-term debt (including current portion)	976	1,109
Less: current portion of long-term debt	(194)	(178)
Total long-term debt	$ 782	$ 931

At September 30, 2010 the Company had a $50 million revolving credit facility with Wells Fargo Bank, National Association (Wells Fargo). The revolving credit facility contains covenants, including covenants relating to liquidity and other financial measurements, and provides for events of default, including failure to pay any interest when due, failure to perform or observe covenants, bankruptcy or insolvency events and the occurrence of a material adverse effect. We have granted Wells Fargo a security interest in substantially all of our assets. We did not draw on the facility during the first nine months of 2010 or during 2009. We have no other significant credit facilities.

12 - Segment, Customer and Geographic Information

We operate in one reportable segment in which we provide healthcare products used for the screening, detection, treatment, monitoring and tracking of common medical ailments in newborn care, hearing impairment, neurological dysfunction, epilepsy, sleep disorders, and balance and mobility disorders.

Our end-user customer base includes hospitals, clinics, laboratories, physicians, nurses, audiologists, and governmental agencies. Most of our international sales are to distributors who resell our products to end-users or sub-distributors.

Revenue and long-lived asset information by geographic region is as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Revenue:				
United States	$ 32,191	$ 30,113	$ 94,261	$ 78,800
Foreign countries	21,088	14,138	60,875	36,071

Totals	$ 53,279	$ 44,251	$ 155,136	$ 114,871

	September 30, 2010	December 31, 2009
Long-lived assets:		
United States	$ 123,603	$ 125,379
Foreign countries	54,360	55,181
Totals	$ 177,963	$ 180,560

Long-lived assets consist principally of property and equipment (net), intangible assets (net), goodwill and non-current inventories. During the three and nine months ended September 30, 2010 and 2009, no single customer or foreign country contributed to more than 10% of revenue, and revenue from services was less than 10% of revenue.

During the three and nine months ended September 30, 2010, respectively, revenue from devices and systems was $30.6 million and $94.3 million, while revenue from supplies and services was $21.7 million and $58.2 million, respectively.

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NATUS MEDICAL INCORPORATED AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited) (Continued)

13 - Fair Value of Financial Instruments

The fair value of our assets and liabilities subject to fair value measurements are as follows (in thousands):

	Fair Value as of September 30, 2010	Fair Value Measurements as of September 30, 2010 Using Fair Value Hierarchy		
		Level 1	Level 2	Level 3
Bank money market investments	$ 3,145		$ 3,145	
Guaranteed investment certificate	982		982	
Total	$ 4,127		$ 4,127	

	Fair Value as of December 31, 2009	Fair Value Measurements as of December 31, 2009 Using Fair Value Hierarchy		
		Level 1	Level 2	Level 3
Bank money market investments	$ 3,142		$ 3,142	
Guaranteed investment certificate	965		965	
Total	$ 4,107		$ 4,107	

In accordance with ASC Topic 820, *Fair Value Measurements*, Level 1 evaluations are based on quoted prices in active markets for identical assets or liabilities that we have the ability to access. Level 2 evaluations are based on quoted prices in markets that are not active or for which all significant inputs are observable, either directly or indirectly. Bank money market accounts have a net asset value of $1.00 per share and are classified as Level 2 assets. Level 3 evaluations are based on assets and liabilities for which there are no observable inputs that are significant to the overall fair value measurement.

14 - Subsequent Events

Acquisition of Medix Industrial y Commercial S.A.

The Company acquired all of the capital stock of Medix Industrial y Commercial S.A. on October 12, 2010 for $14 million in cash, excluding direct costs of the acquisition, with the potential for additional purchase consideration if certain revenue targets are met in 2011 and 2012. Medix is a leader in the development, manufacturing, and sales of devices for newborn care in Latin America. Medix, based in Argentina, manufactures incubators for use in hospital nurseries and neonatal intensive care units, transport incubators for use in ambulances and other emergency vehicles, infant warmers, and LED based phototherapy devices.

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ITEM 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

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Overview

The following Management s Discussion and Analysis of Financial Condition and Results of Operations (MD&A) supplements the MD&A in the Annual Report on Form 10-K for the year ended December 31, 2009 of Natus Medical Incorporated (Natus, we, us, or our Company), and presumes that readers have read or have access to the discussion and analysis in our Annual Report. Management s discussion and analysis should be read in conjunction with our condensed consolidated financial statements and accompanying footnotes, the discussion of certain risks and uncertainties contained in Part II, Item 1A of this report, and the cautionary information regarding forward-looking statements at the end of this section. MD&A includes the following sections:

Our Business. A general description of our business;

2010 Third Quarter Overview. A summary of key information concerning the financial results for the three months ended September 30, 2010;

Application of Critical Accounting Policies. A discussion of the accounting policies that are most important to the portrayal of our financial condition and results of operations and that require significant estimates, assumptions, and judgments;

Results of Operations. An analysis of our results of operations for the periods presented in the financial statements;

Liquidity and Capital Resources. An analysis of capital resources, sources and uses of cash, investing and financing activities, off-balance sheet arrangements, contractual obligations and interest rate hedging;

Recent Accounting Pronouncements. See Note 1 to our Condensed Consolidated Financial Statements for a discussion of new accounting pronouncements that affect us; and

Cautionary Information Regarding Forward-Looking Statements. Cautionary information about forward-looking statements.

Our Business

Natus is a leading provider of healthcare products used for the screening, detection, treatment, monitoring and tracking of common medical ailments in newborn care, hearing impairment, neurological dysfunction, epilepsy, sleep disorders, and balance and mobility disorders. Product offerings include computerized neurodiagnostic systems for audiology, neurology, polysomnography, and neonatology, as well as newborn care products such as hearing screening systems, phototherapy devices for the treatment of newborn jaundice, head-cooling products for the treatment of brain injury in newborns, and software systems for managing and tracking disorders and diseases for public health laboratories.

We have completed a number of acquisitions since 2003, consisting of either the purchase of a company, substantially all of the assets of a company, or individual products or product lines. The businesses we have acquired are Neometrics in 2003, Fischer-Zoth in 2004, Bio-logic, Deltamed, and Olympic Medical in 2006, Xltek in 2007, Sonamed, Schwarzer Neurology, and Neurocom in 2008, and Hawaii Medical and Alpine Biomed in 2009. We acquired Medix after the close of the third quarter of 2010.

Product Families

We categorize our products into the following product families, which are more fully described in our Annual Report on Form 10-K for the year ended December 31 2009:

Hearing Includes products for newborn hearing screening and diagnostic hearing assessment.

Monitoring Systems for Neurology Includes products for diagnostic electroencephalography (EEG), diagnostic sleep analysis (PSG), electromyography (EMG), intra-operative monitoring (IOM), newborn brain monitoring, and assessment of balance and mobility disorders.

Newborn Care Includes products for the treatment of brain injury and jaundice in newborns.

Segment and Geographic Information

We operate in one reportable segment in which we provide healthcare products used for the screening, detection, treatment, monitoring and tracking of common medical ailments in newborn care, hearing impairment, neurological dysfunction, epilepsy, sleep disorders, and balance and mobility disorders.

Our end-user customer base includes hospitals, clinics, laboratories, physicians, nurses, audiologists, and governmental agencies. Most of our international sales are to distributors who resell our products to end-users or sub-distributors.

Information regarding our sales and long-lived assets in the U.S. and in countries outside the U.S. is contained in Note 12 *Segment, Customer and Geographic Information* of our condensed consolidated financial statements included in this report.

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Revenue by Product Category

We generate our revenue either from sales of Devices and Systems, which are generally non-recurring, and from related Supplies and Services, which are generally recurring. The products that are attributable to these categories are described in our Annual Report on Form 10-K for the year ended December 31, 2009. Revenue from Devices and Systems and Supplies and Services, as a percent of total revenue for the three and nine months ended September 30, 2010 and 2009 is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Devices and Systems	57%	54%	61%	55%
Supplies and Services	41%	44%	37%	43%
Other	2%	2%	2%	2%
Total	100%	100%	100%	100%

During the three and nine months ended September 30, 2010 and 2009, no single customer or foreign country contributed to more than 10% of revenue, and revenue from services was less than 10% of revenue.

2010 Third Quarter Overview

Our revenue increased 20% to $53.3 million in the third quarter ended September 30, 2010, compared to $44.3 million in the comparable quarter of the previous year. Net income was $3.7 million, or $0.13 per diluted share, for both the third quarter of 2010 and 2009. Alpine Biomed contributed to $5.8 million of the increase; in addition, revenue from our existing product lines increased 5% in the 2010 period, including a significant increase in revenue from our newborn hearing screening devices. Gross profit was 1.6% lower for the third quarter of 2010 compared to the third quarter of 2009, reflecting higher material costs, increased charges for inventory obsolescence, and a charge associated with discontinuance of the Sonamed Clarity product line.

During the third quarter of 2010 we received a purchase order from the Kingdom of Saudi Arabia for our newborn care products. The order, which is valued at over $2.9 million, is for ALGO newborn hearing screeners, Cool-Cap selective head-cooling devices, Olympic Cerebral Functions Monitors (CFM), and associated disposable supplies. We shipped approximately $2.0 million of the order in the third quarter and expect to ship the remainder of the order in the fourth quarter.

Our new Xltek Protektor32 IOM system received FDA 510(k) approval following nearly two years of product development. The product s features include: 64 software switchable inputs, 128 channel display, transcranial motor evoked potential (TcMEP) stimulator, pulse oximetry recording, mixed mode EMG, and automatic recovery from EMI events common in the operating room. We started limited market release testing during the third quarter and expect a full product release in the fourth quarter.

Application of Critical Accounting Policies

We prepare our financial statements in accordance with accounting principles generally accepted in the United States of America (GAAP). In so doing, we must often make estimates and use assumptions that can be subjective, and, consequently, our actual results could differ from those estimates. For any given individual estimate or assumption we make, there may also be other estimates or assumptions that are reasonable.

We believe that the following critical accounting policies require the use of significant estimates, assumptions, and judgments. The use of different estimates, assumptions, or judgments could have a material affect on the reported amounts of assets, liabilities, revenue, expenses, and related disclosures as of the date of the financial statements and during the reporting period:

Revenue recognition

Allowance for doubtful accounts

Inventory is carried at the lower of cost or market value

Carrying value of intangible assets and goodwill

Liability for product warranties

Share-based compensation

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These critical accounting policies are described in more detail in our Annual Report on Form 10-K for the year ended December 31, 2009, under Item 7, *Management s Discussion and Analysis of Financial Condition and Results of Operations*. Other than as noted in Note 1 of the Notes to Consolidated Financial Statements (unaudited) contained in Item 1 of this quarterly report on Form 10-Q addressing changes to our policies for revenue recognition, there have been no changes to these policies during the three and nine months ended September 30, 2010.

Results of Operations

The following table sets forth, for the periods indicated selected consolidated statements of operations data as a percentage of total revenue. Our historical operating results are not necessarily indicative of the results for any future period.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Revenue	100.0%	100.0%	100.0%	100.0%
Cost of revenue	41.0%	39.4%	40.6%	39.1%
Gross profit	59.0%	60.6%	59.4%	60.9%
Operating expenses:				
Marketing and selling	23.8%	26.6%	25.8%	27.9%
Research and development	9.0%	9.4%	9.8%	10.3%
General and administrative	15.2%	12.9%	17.3%	14.3%
Total operating expenses	48.0%	48.9%	52.9%	52.5%
Income from operations	11.0%	11.7%	6.5%	8.4%
Other income (expense), net	(0.3)%	0.2%	0.0%	0.5%
Income before provision for income tax	10.7%	11.9%	6.5%	8.9%
Provision for income tax	3.6%	3.6%	2.3%	3.0%
Net income	7.1%	8.3%	4.2%	5.9%

We acquired Hawaii Medical in July 2009 and Alpine Biomed in September 2009. Where significant, we have noted the impact of these acquisitions on our results of operations for the three and nine months ended September 30, 2010, as compared to the same periods in 2009.

Three Months Ended September 30, 2010 and 2009

Our revenue increased 20%, or $9.0 million, to $53.3 million for the three month period ended September 30, 2010 compared to $44.3 million in the comparable 2009 period. Revenue of Alpine Biomed contributed to $5.8 million of the increase, while revenue from our newborn care products increased by $2.6 million to $9.4 million, and revenue from our newborn hearing products increased $1.1 million to $18.3 million.

Revenue from devices and systems increased $6.9 million, or 29%, to $30.6 million in the three months ended September 30, 2010, compared to $23.8 million in the same period in 2009. Revenue from Alpine Biomed contributed to $3.8 million of the increase, while revenue from our other neurology products contributed to $1.8 million of the increase and revenue from newborn hearing screening and newborn care contributed to $2.5 million of the increase, offset by a $1.2 million decrease in sleep diagnostics and balance monitoring products. Revenue from devices and systems was 57% of total revenue in the three months ended September 30, 2010 compared to 54% of total revenue for the third quarter of

2009.

Revenue from supplies and services increased 10%, or $2.0 million, to $21.7 million in the third quarter of 2010 compared to $19.7 million in the same period in 2009. In the 2010 third quarter, revenue from hearing screening and neurology supplies increased by $2.7 million and revenue from newborn care supplies increased by $500,000 offset by a $1.2 million decrease in service fee revenue. Revenue from supplies and services was 41% of total revenue in the three months ended September 30, 2010 compared to 44% of total revenue for the third quarter of 2009.

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Revenue from sales outside the U.S. increased 49%, or $7.0 million, to $21.1 million in the third quarter of 2010 compared to $14.1 million for the same period in 2009. Revenue from Alpine Biomed contributed to $5.1 million of the increase while revenue from our hearing screening and newborn care devices increased $1.9 million including $2.0 million attributable to the Saudi Arabia order.

Gross profit as a percentage of revenue was 59.0% for the three months ended September 30, 2010 compared to 60.6% for the respective period in 2009, reflecting higher materials costs, a charge associated with discontinuance of the Sonamed Clarity product line that reduced gross profit by 0.6 percentage points and higher than normal charges for inventory obsolescence. Gross profit increased $4.6 million, or 17%, to $31.4 million in 2010 from $26.8 million in 2009.

Total operating costs increased by $4.0 million or 18%, to $25.6 million in the three months ended September 30, 2010, compared to $21.6 million in the same period in 2009. The operations of Alpine Biomed contributed to $1.4 million of the increase. The net increase in total operating costs was also attributable to increases in payroll, related benefit costs, outside consulting services and travel and related expenses to support the increase in revenue.

Marketing and selling expenses increased $926,000, or 8%, to $12.7 million in the three months ended September 30, 2010, compared to $11.8 million in the same period in 2009. The expenses of Alpine Biomed contributed to $655,000 of the increase. The remainder of the increase was primarily attributable to higher travel and related costs.

Research and development expenses increased $645,000, or 15%, to $4.8 million for the three months ended September 30, 2010, compared to $4.2 million in the same period of 2009. The operations of Alpine Biomed contributed to $498,000 of the increase, while other research and development expenses were marginally higher in the third quarter of 2010 compared to the same period in 2009.

General and administrative expenses increased $2.4 million, or 42%, to $8.1 million in the three months ended September 30, 2010, compared to $5.7 million in the same period in 2009. The operations of Alpine Biomed contributed to $231,000 of the increase. Other general and administrative expenses exclusive of those associated with Alpine Biomed were $2.2 million higher in the 2010 third quarter compared to the same period in 2009, which resulted primarily from increased payroll, related benefit costs, outside consulting costs, travel and related expenses, and amortization of internally developed software.

Other income (expense), net, consists of investment income from our investment portfolio, interest expense, net currency exchange gains and losses, and other miscellaneous income and expenses. We reported net other expense of $175,000 in the three months ended September 30, 2010, compared to net other income of $71,000 in the same period in 2009. During the 2010 period we generated $34,000 of investment income compared to $40,000 in the 2009 period. We also recognized $280,000 of foreign exchange losses compared with $183,000 of foreign exchange gains during the three months ended September 30, 2010 and 2009 respectively, reflecting the weakening US dollar against the euro.

We recorded a provision for income taxes of $1.9 million in the three months ended September 30, 2010, compared to $1.6 million in the same period in 2009. Our effective tax rate in the third quarter of 2010 was 34.2% compared to an effective rate of 30.0% in the third quarter of 2009 primarily because in the quarter ending September 30, 2010, we did not receive a tax benefit from our Canadian subsidiary related to foreign exchange gains which we benefited from during the quarter ending September 30, 2009.

Nine Months Ended September 30, 2010 and 2009

Revenue increased $40.3 million, or 35%, to $155.1 million for the nine month period ended September 30, 2010 compared to $114.9 million in the comparable 2009 period. Revenue of Alpine Biomed and Hawaii Medical contributed to $23.9 million of the increase, while revenue from our hearing and newborn care products increased by $7.7 million to $78.6 million, and revenue from our neurology products other than from Alpine Biomed increased $8.6 million to $70.5 million.

Device and systems revenue increased $30.7 million, or 48%, to $94.3 million in the nine months ended September 30, 2010 compared to $63.6 million in the same period in 2009. Revenue from Alpine Biomed contributed to $14.5 million of the increase, while revenue from our hearing and newborn care products contributed to $9.6 million of the increase, and revenue from our other neurology products, exclusive of sleep diagnostics and balance monitoring products, contributed to $8.7 million of the increase, offset by a $2.1 million decrease in sleep diagnostics and balance monitoring products. Revenue from devices and systems was 61% of consolidated revenue in the nine months ended September 30, 2010 compared to 55% of consolidated revenue for the first nine months of 2009.

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Supplies and services revenue increased $9.1 million, or 19%, to $58.2 million in the nine months ended September 30, 2010 compared to $49.0 million in the same period in 2009. Alpine Biomed contributed to $6.1 million of revenue from supplies and services while supplies and service revenue from other products increased $3.0 million. Revenue from supplies and services was 37% of consolidated revenue in the nine months ended September 30, 2010 compared to 43% of consolidated revenue for the nine months ended September 30, 2009.

Revenue from sales outside the U.S. increased $24.8 million, or 69%, to $60.9 million in the first nine months of 2010 compared to $36.1 million for the same period in 2009. Revenue from Alpine Biomed contributed to $17.9 million of the increase in international revenue, while revenue from our hearing screening devices increased $2.9 million and newborn care products increased $3.2 million in international markets. Revenue from supplies and services, exclusive of Alpine Biomed, increased by $1.2 million or 10%, in international markets.

Gross profit as a percentage of revenue was 59.4% for the nine months ended September 30, 2010 compared to 60.9% for the respective period in 2009. Cost of revenue increased $18.1 million, or 40%, to $63.0 million in the nine months ended September 30, 2010, from $44.9 million in 2009, reflecting increased sales in the 2010 period coupled with higher material costs and charges associated with discontinuance of the Sonamed Clarity product line that reduced gross profit by 0.9 percentage points. Gross profit increased $22.2 million, or 32%, to $92.2 million in 2010 from $70.0 million in 2009.

Total operating costs increased by $21.7 million or 36%, to $82.0 million in the nine months ended September 30, 2010, compared to $60.3 million in the same period in 2009. The operations of Alpine Biomed contributed to $10.9 million of the increase. The net increase in total operating costs was also attributable to increases in employee compensation and outside consulting costs to support the increase in revenue.

Marketing and selling expenses increased $8.0 million, or 25%, to $40.0 million in the nine months ended September 30, 2010 compared to $32.0 million in the same period in 2009. The expenses of Alpine Biomed contributed to $5.0 million of the increase. The remainder of the increase was primarily attributable to higher sales commission costs and travel related costs associated with the increase in our revenue.

Research and development expenses increased $3.4 million, or 28%, to $15.2 million in the nine months ended September 30, 2010 compared to $11.8 million in the same period of 2009. The operations of Alpine Biomed contributed to $2.7 million of the increase, while the remainder of the increase resulted primarily from higher outside service costs.

General and administrative expenses increased $10.3 million, or 63%, to $26.8 million in the nine months ended September 30, 2010 compared to $16.5 million in the same period in 2009. The operations of Alpine Biomed contributed to $3.2 million of the increase. We also recorded a restructuring charge of $3.1 million in the first nine months of 2010 for which there was no comparable cost in 2009. Other general and administrative expenses exclusive of those associated with Alpine Biomed were $3.6 million higher in the 2010 first nine months compared to the same period in 2009, which resulted primarily from increased payroll, related benefit costs, travel and outside consulting costs.

Other income (expense), net consists of investment income from our investment portfolio, interest expense, net currency exchange gains and losses, and other miscellaneous income and expenses. We reported net other income of $11,000 in the nine months ended September 30, 2010, compared to $584,000 in the same period in 2009. During the 2010 period we generated $30,000 of investment income compared to $218,000 in the 2009 period due to lower rates of interest on our investment portfolio. We also recognized $647,000 of foreign exchange losses compared with $159,000 of foreign exchange gains during the nine months ended September 30, 2010 and 2009 respectively, reflecting the weakening US dollar against the euro.

We recorded income tax expense of $3.6 million in the nine months ended September 30, 2010, compared to $3.5 million in the same period in 2009. Our effective tax rate in the first nine months of 2010 was 35.7% compared to an effective rate of 33.9% in the same period in 2009.

Liquidity and Capital Resources

Liquidity is our ability to generate sufficient cash flows from operating activities to meet our obligations and commitments. In addition, liquidity includes the ability to obtain appropriate financing and to raise capital. Therefore, liquidity cannot be considered separately from capital resources that consist of our current funds and the potential to increase those funds in the future. We plan to use these resources in meeting our commitments and in achieving our business objectives.

As of September 30, 2010, we had cash, cash equivalents, and short-term investments of $43.5 million, stockholders equity of $256.1 million, and working capital of $91.0 million, compared with cash, cash equivalents, and short-term investments of $33.5 million, stockholders equity of $243.2 million, and working capital of $75.0 million as of December 31, 2009.

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We believe that our current cash and cash equivalents and any cash generated from operations will be sufficient to meet our ongoing operating and capital requirements for the foreseeable future. We completed two acquisitions in 2009 including Alpine Biomed at the end of the third quarter, four acquisitions in 2008, one in 2007, and three in 2006. We intend to continue to acquire additional technologies, products, or businesses and these acquisitions could be significant. These actions would likely affect our future capital requirements and the adequacy of our available funds. In order to finance future acquisitions, we may be required to raise additional funds through public or private financings, strategic relationships or other arrangements. Any equity financing may be dilutive to stockholders, and debt financing, if available, may involve restrictive covenants and increase our cost of capital.

At September 30, 2010 we had a $50 million revolving credit facility with Wells Fargo Bank, National Association (Wells Fargo). The revolving credit facility contains covenants, including covenants relating to liquidity and other financial measurements, and provides for events of default, including failure to pay any interest when due, failure to perform or observe covenants, bankruptcy or insolvency events and the occurrence of a material adverse effect. We have granted Wells Fargo a security interest in substantially all of our assets. We did not draw on the facility during the first nine months of 2010 or during 2009. We have no other significant credit facilities.

On October 12, 2010, we acquired all outstanding shares of Medix for a cash price paid of $14 million with the potential for additional earnout consideration of up to $5 million if certain post-acquisition sales targets are met. Financing for the transaction was provided by Natus existing cash balances, and based on cash and short-term investments held at September 30, 2010, Natus retains cash of approximately $29 million before giving any effect to potential earnout payments in the transaction.

Global capital markets have been, and may continue to be, disrupted and volatile. The cost and availability of equity and debt funding has been and may continue to be adversely affected by illiquid capital and credit markets. Some lenders have reduced or, in some cases, ceased to provide funding to borrowers. We believe that we have adequate liquidity to meet our present needs. Turbulence in the United States and international financial markets, however, could adversely affect the cost and availability of financing to us in the future and limit our ability to acquire products, other assets, or businesses.

Cash provided by operations decreased by $11.3 million for the nine months ended September 30, 2010 to $9.6 million, compared to $20.9 million for the same period in 2009. The sum of our net income and certain non-cash expense items, such as reserves, depreciation and amortization, and share based compensation was approximately $17.1 million in the 2010 period, compared to $17.9 million in 2009. In addition, in the 2010 period we paid approximately $3.1 million of severance benefits associated with a reorganization plan we adopted in January 2010 for which there was no similar expenditure in 2009. The overall impact of changes in certain operating assets and liabilities on total operating cash flows resulted in a cash outflow of $7.5 million in 2010 compared with a cash inflow of $3.0 million in 2009. In particular, our cash flow from operations in the first nine months of 2010 was affected by a $3.1 million decrease in accounts payable, accrued expenses and other liabilities coupled with a $6.0 million increase in inventories.

Cash used in investing activities was $2.8 million for the nine months ended September 30, 2010, compared to $50.6 million for the same period in 2009. In the 2009 period, we acquired Hawaii Medical and Alpine Biomed at a cost of $46.5 million for which there were no similar expenditures in 2010. We used $2.6 million and $1.9 million of cash to acquire property and equipment during the nine months ended September 30, 2010 and 2009, respectively, and capitalized $215,000 of internal use software development costs in 2010 compared to $637,000 in 2009.

Cash provided by financing activities was $2.5 million in the nine months ended September 30, 2010, compared to $188,000 in the same period of 2009. We received cash from sales of our stock pursuant to our stock options and our employee stock purchase plan in the amount of $2.0 million and $542,000 in the nine months ended September 30, 2010 and 2009, respectively. In 2010, we realized an excess tax benefit of $574,000 on the exercise of employee stock options that was recorded as an increase to stockholders equity, as compared with a tax benefit of $31,000 in the first nine months of 2009.

Our future liquidity and capital requirements will depend on numerous factors, including the:

- Extent to which we make acquisitions;

Amount and timing of revenue;

Extent to which our existing and new products gain market acceptance;

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Cost and timing of product development efforts and the success of these development efforts;

Cost and timing of marketing and selling activities; and

Availability of borrowings under line of credit arrangements and the availability of other means of financing.

Commitments and Contingencies

In the normal course of business, we enter into obligations and commitments that require future contractual payments. The commitments primarily result from firm, noncancellable purchase orders placed with contract vendors that manufacture some of the components used in our medical devices and related disposable supply products, as well as commitments for leased office, manufacturing, and warehouse facilities. There have been no material changes to the table of contractual obligations presented in Item 7, *Management s Discussion and Analysis of Financial Condition and Results of Operations*, of our Annual Report on Form 10-K for the year ended December 31, 2009.

Under our bylaws, we have agreed to indemnify our officers and directors for certain events or occurrences arising as a result of the officer or director serving in such capacity. We have a directors and officers liability insurance policy that limits our exposure and enables us to recover a portion of any amounts paid resulting from the indemnification of our directors and officers. In addition, we enter into indemnification agreements with other parties in the ordinary course of business. We believe the estimated fair value of these indemnification agreements is minimal and we have not recorded a liability for these agreements.

Recent Accounting Pronouncements

See Note 1 to our Condensed Consolidated Financial Statements for a discussion of new accounting pronouncements that affect us.

Cautionary Information Regarding Forward Looking Statements

This report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 about Natus Medical Incorporated. These statements include, among other things, statements concerning our expectations, beliefs, plans, intentions, future operations, financial condition and prospects, and business strategies. The words may, will, continue, estimate, project, intend, believe, expect, anticipate, and other similar expressions generally identify forward-looking statements. Forward-looking statements in this Item 2 include, but are not limited to, statements regarding the following: our our belief that the recovery from the worldwide economic downturn has continued, our expectation regarding expansion of our international operations, our expectations regarding our new products, the sufficiency of our current cash, cash equivalents, and short-term investment balances, and any cash generated from operations to meet our ongoing operating and capital requirements for the foreseeable future, our expectations as to the necessity of earnout payments related to our recent acquisitions, our expectation that our deferred tax assets will be fully realized, and our intent to acquire additional technologies, products, or businesses.

Forward-looking statements are not guarantees of future performance and are subject to substantial risks and uncertainties that could cause the actual results predicted in the forward-looking statements as well as our future financial condition and results of operations to differ materially from our historical results or currently anticipated results. Investors should carefully review the information contained under the caption Risk Factors contained in Part II, Item 1A of this report for a description of risks and uncertainties. All forward-looking statements are based on information available to us on the date hereof, and we assume no obligation to update forward-looking statements.

ITEM 3. Quantitative and Qualitative Disclosures about Market Risk

We develop products in the U.S., Canada, and Europe and sell those products primarily in the U.S., Europe and Asia. As a result, our financial results could be affected by factors such as changes in foreign currency exchange rates or weak economic conditions in foreign markets. Most of our sales in Europe and Asia are denominated in U.S. dollars and Euros, and with the acquisition of Xltek in November 2007, a small portion of our sales are now denominated in Canadian dollars. As our sales in currencies other than the U.S. dollar increase, our exposure to foreign currency fluctuations may increase.

In addition, changes in exchange rates also may affect the end-user prices of our products compared to those of our foreign competitors, who may be selling their products based on local currency pricing. These factors may make our products less competitive in some countries.

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If the U.S. dollar uniformly increased or decreased in strength by 10% relative to the currencies in which our sales were denominated, our net income would have correspondingly increased or decreased by an immaterial amount for the nine months ended September 30, 2010. Our interest income is sensitive to changes in the general level of interest rates in the U.S. However, because recent market conditions have resulted in historically low rates of return on our investments, a hypothetical decrease of 10% in market interest rates would not result in a material decrease in interest income earned on our investments held as of September 30, 2010.

When able, we invest excess cash in bank money-market funds or discrete short-term investments. The fair value of short-term investments and cash equivalents (investments) is sensitive to changes in the general level of interest rates in the U.S., and the fair value of these investments will fall if market interest rates increase. However, since we generally have the ability to hold these investments to maturity, these declines in fair value may never be realized. If market interest rates were to increase by 10% from levels at September 30, 2010, the fair value of our investments would decline by an immaterial amount.

All of the potential changes noted above are based on sensitivity analyses performed on our financial position as of September 30, 2010. Actual results may differ as our analysis of the effects of changes in interest rates does not account for, among other things, sales of securities prior to maturity and repurchase of replacement securities, the change in mix or quality of the investments in the portfolio, and changes in the relationship between short-term and long-term interest rates.

ITEM 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Under the rules of the Securities and Exchange Commission, disclosure controls and procedures are controls and other procedures that are designed to ensure that information required to be disclosed in the reports that we file or submit 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. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by us in our reports that we file or submit under the Securities Exchange Act of 1934 is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate, to allow timely decisions regarding required disclosure.

Our management, with the participation of our chief executive officer and our chief financial officer, has evaluated the effectiveness of our disclosure controls and procedures as of September 30, 2010. Our chief executive officer and chief financial officer determined that as of September 30, 2010 our disclosure controls and procedures were effective for the purpose set forth above.

Changes in Internal Control over Financial Reporting

Under the rules of the Securities and Exchange Commission, internal control over financial reporting is defined as a process designed by, or under the supervision of, an issuer s principal executive and principal financial officers, and effected by the issuer s board of directors, management and other personnel, to provide reasonable assurances regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

There was no change in our internal control over financial reporting that occurred during the fiscal quarter ended September 30, 2010, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings

We may from time to time become a party to various legal proceedings or claims that arise in the ordinary course of business. Our management reviews these matters if and when they arise and believes that the resolution of any of these matters will not have a significant adverse effect on our financial condition.

ITEM 1A. Risk Factors

We have completed a number of acquisitions and expect to complete additional acquisitions in the future. There are numerous risks associated with acquisitions and we may not achieve the expected benefit of any of our acquisitions

Our acquisitions of products, technology assets, or businesses may have a negative impact on our business if we fail to achieve the anticipated financial, strategic, and other benefits of acquisitions or investments, and our operating results may suffer because of this.

Our significant acquisitions are as follows: Neometrics in 2003; Fischer-Zoth in 2004; Bio-logic, Deltamed, and Olympic in 2006; Xltek in 2007; Sonamed, Schwarzer Neurology, and Neurocom in 2008; Hawaii Medical and Alpine Biomed in 2009, and Medix in 2010.

We expect to continue to pursue opportunities to acquire other businesses in future periods. The acquisitions that we have completed may not result in improved operating results for us, or in our achieving a financial condition superior to that which we would have achieved had we not completed them. Our results of operations may be adversely impacted by costs associated with our acquisitions, including one-time charges associated with restructurings. Further, our acquisitions could fail to produce the benefits that we anticipate, or could have other adverse effects that we currently do not foresee. In addition, some of the assumptions that we have relied upon, such as achievement of operating synergies, may not be realized. In this event, one or more of the acquisitions could result in reduced earnings of Natus as compared to the earnings that would have been achieved by Natus if the acquisition had not occurred.

We have assumed contingent obligations associated with earnout provisions in some of our acquisitions. We believe these provisions help us to negotiate mutually agreeable purchase terms between us and the sellers. However, a disagreement between us and a seller about the terms of an earnout provision could result in our paying more for an acquisition then we intended. For example, such a disagreement arose in connection with our acquisition of Alpine Biomed, which we have subsequently resolved. The stockholders of Schwarzer Neurology have recently asserted claims relating to the earnout provision of our agreement with those stockholders that have not yet been resolved. Disputes over these types of contingent obligations may not be resolved on terms that are favorable to us and the payment of additional purchase consideration could impact our results of operations and financial position.

We have incurred indebtedness to fund some of our acquisitions. The use of debt to fund our acquisitions may have an adverse impact on our liquidity and cause us to place more reliance on cash flow from operations for our liquidity. If our cash flow from operations is not sufficient for our needs, our business could be adversely affected. If we are required to seek additional external financing to support our need for cash to fund future acquisitions, we may not have access to financing on terms that are acceptable to us, or at all. Alternatively, we may feel compelled to access additional financing on terms that are dilutive to existing holders of our common stock or that include covenants that restrict our business, or both. If the recent lack of liquidity in credit markets persists into the future, our ability to obtain debt financing for future acquisitions may be impaired.

If we fail to successfully manage the combined operations of Natus and the businesses we have acquired, we may not realize the potential benefits of our acquisitions. Our corporate headquarters are located in San Carlos, California. We also have the following operating divisions: Olympic in Washington; Neurocom in Oregon; Bio-logic in Illinois; Neometrics in New York; Xltek and Stellate in Canada; Medix in Argentina; Alpine Biomed in Denmark; Fischer-Zoth, Schwarzer Neurology, and IT-Med (collectively Natus Europe) and Alpine Biomed Germany in Germany; and Deltamed and Alpine Biomed France in France. If we fail to manage these disparate operations effectively, our results of operations could be harmed, employee morale could decline, key employees could leave, and customers could cancel existing orders or choose not to place new ones. In addition, we may not achieve the synergies or other benefits of these and future acquisitions that we anticipate. We may encounter the following additional difficulties and delays involved in integrating and managing these operations, and the

operations of companies we may acquire:

Failure of customers to continue using the products and services of the combined company;

Failure to successfully develop the acquired technology into the desired products or enhancements;

Assumption of unknown liabilities;

Failure to understand products or technologies with which we have limited previous experience;

Failure to compete effectively in new markets;

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Decreased liquidity, restrictive bank covenants, and incremental financing costs associated with debt we may incur to complete future acquisitions; and

Diversion of the attention of management from other ongoing business concerns.

Our acquisitions of products, technology assets, or businesses may have a negative impact on our business if we fail to achieve the anticipated financial, strategic and other benefits of these acquisitions or investments. In addition, our reported operating results may suffer because of impairment charges incurred to write down the carrying amount of intangible assets, including goodwill, generated as a result of the acquisitions.

Adverse economic conditions in markets in which we operate may harm our business

Unfavorable changes in U.S. and international economic environments may adversely affect our business and financial results. Economic conditions in the countries in which we operate and sell products worsened and global financial markets subsequently experienced significant volatility and declines throughout much of 2009. We are unable to foresee when, or if, these factors might return to more normal levels. During challenging economic times, and in tight credit markets, our customers may delay or reduce capital expenditures. This could result in reductions in sales of our products, longer sales cycles, difficulties in collection of accounts receivable, slower adoption of new technologies, and increased price competition, all of which could impact our results of operations and financial condition. In addition, we expect these factors will cause us to be more cautious in evaluating potential acquisition opportunities, which could hinder our ability to grow through acquisition while these conditions persist.

Our growth in recent years has depended substantially on the completion of acquisitions and we may not be able to complete acquisitions of this nature or of a relative size in the future to support a similar level of growth

The acquisitions that we have completed have been the primary source of our growth in revenue in recent years. We expend considerable effort in seeking to identify attractive acquisition candidates and, upon doing so, to convince the potential target to consider a sale to us and, ultimately, to negotiate mutually agreeable acquisition terms. If we are not successful in these efforts in the future, our growth rate will not increase at a rate corresponding to that which we have achieved in recent years. Further, as we grow larger it will be necessary to complete the acquisition of larger companies and product lines to support a growth similar to that which we have achieved in the past. The market for attractive acquisitions is competitive and others with greater financial resources than we have may be better positioned than we are to acquire desirable targets. Further, we may not be able to negotiate acquisition terms with target companies that will allow us to achieve positive financial returns from the transaction.

We have initiated changes to our information systems that could disrupt our business and our financial results.

We plan to continuously improve our enterprise resource planning, customer relationship management, and document lifecycle management systems to support the form, functionality, and scale of our business. These types of transitions frequently prove disruptive to the underlying business of an enterprise and may cause us to incur higher costs than we anticipate. Failure to manage a smooth transition to the new systems and the ongoing operations and support of the new systems could materially harm our business operations.

For example, we are currently in the process of implementing the rollout of an enterprise resource planning application (ERP) in our European operating divisions. Until we have completed this ERP implementation, we will be dependent on multiple platforms. We may experience difficulties in implementing the ERP and we may fail to gain the efficiencies the implementation is designed to produce. The implementation could also be disruptive to our operations, including the ability to timely ship and track product orders to customers, project inventory requirements, manage our supply chain and otherwise adequately service our customers**.**

Future changes in technology or market conditions could result in adjustments to our recorded asset balance for intangible assets, including goodwill, resulting in additional charges that could significantly impact our operating results

Our balance sheet includes significant intangible assets, including goodwill and other acquired intangible assets. The determination of related estimated useful lives and whether these assets are impaired involves significant judgments. Our ability to accurately predict future cash flows related to these intangible assets might be hindered by events over which we have no control. Due to the highly competitive nature of the medical device industry, new technologies could impair the value of our intangible assets if they create market conditions that adversely affect the competitiveness of our products. Any future determination that these assets are carried at greater than their fair value could result in substantial impairment charges, which could significantly impact our operating results.

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We may not be able to preserve the value of our intellectual property because we may not be able to protect access to it or we may lose our intellectual property rights due to expiration of our licenses or patents

If we fail to protect our intellectual property rights or if our intellectual property rights do not adequately cover the technology we employ, other medical device companies could sell products with features similar to ours, and this could reduce demand for our products. We protect our intellectual property through a combination of patent, copyright, trade secret and trademark laws. Despite our efforts to protect our proprietary rights, others may attempt to copy or otherwise improperly obtain and use our products or technology. Policing unauthorized use of our technology is difficult and expensive, and we cannot be certain that the steps we have taken will prevent misappropriation. Our means of protecting our proprietary rights may be inadequate. Enforcing our intellectual property rights could be costly and time consuming and may divert our management s attention and resources. Failing to enforce our intellectual property rights could also result in the loss of those rights.

If health care providers are not adequately reimbursed for procedures conducted with our devices or supplies, or if reimbursement policies change adversely, we may not be successful marketing and selling our products or technologies

Clinicians, hospitals, and government agencies are unlikely to purchase our products if clinicians are not adequately reimbursed for the procedures conducted with our devices or supplies. Unless a sufficient amount of conclusive, peer-reviewed clinical data about our products has been published, third-party payors, including insurance companies and government agencies, may refuse to provide reimbursement. Furthermore, even if reimbursement is provided, it may not be adequate to fully compensate the clinicians or hospitals. Some third-party payors may impose restrictions on the procedures for which they will provide reimbursement. If health care providers cannot obtain sufficient reimbursement from third-party payors for our products or the screenings conducted with our products, we may not achieve significant market acceptance of our products. Acceptance of our products in international markets will depend upon the availability of adequate reimbursement or funding within prevailing healthcare payment systems. Reimbursement, funding, and healthcare payment systems vary significantly by country. We may not obtain approvals for reimbursement in a timely manner or at all.

Adverse changes in reimbursement policies in general could harm our business. We are unable to predict changes in the reimbursement methods used by third-party health care payors, particularly those in countries and regions outside the U.S. For example, some payors are moving toward a managed care system in which providers contract to provide comprehensive health care for a fixed cost per person. In a managed care system the cost of our products may not be incorporated into the overall payment for patient care or there may not be adequate reimbursement for our products separate from reimbursement for other procedures.

Healthcare reforms, changes in healthcare policies, and changes to third-party reimbursements for our products may affect demand for our products

In March 2010 the U. S. government signed into law the *Patient Protection and Affordable Care Act* and the *Health Care & Education Reconciliation Act*. These laws are intended to, among other things, curb rising healthcare costs, including those that could significantly affect reimbursement for our products. The policies supporting these laws include: basing reimbursement policies and rates on clinical outcomes; the comparative effectiveness and costs of different treatment technologies and modalities; imposing price controls; and other measures. Future significant changes in the healthcare systems in the United States or elsewhere could also have a negative impact on the demand for our current and future products. These include changes that may reduce reimbursement rates for our products and changes that may be proposed or implemented by the current U.S. Presidential administration or Congress.

There are numerous steps required to implement these laws. Because of the unsettled nature of these reforms, we cannot predict what additional healthcare reforms will be implemented at the federal or state level, or the effect that any future legislation or regulation will have on our business. There is also considerable uncertainty of the impact of these reforms on the medical device market as a whole. If we fail to effectively react to the implementation of health care reform, our business may be adversely affected. In addition, if the excise tax on the sale of medical devices is imposed as enacted, this could increase our costs and have an adverse effect on our results of operations, financial position, and cash flows.

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If we fail in our efforts to educate clinicians, government agency personnel, and third-party payors on the effectiveness of our products, we may not achieve future sales growth

It is critical to the success of our sales efforts that we educate a sufficient number of clinicians, hospital administrators, and government agencies about our products and the costs and benefits of their use. The commercial success of our products depends upon clinician, government agency and other third-party payor confidence in the economic and clinical benefits of our products as well as their comfort with the efficacy, reliability, sensitivity and specificity of our products. We believe that clinicians will not use our products unless they determine, based on published peer-reviewed journal articles and experience, that our products provide an accurate and cost-effective alternative to other means of testing or treatment. Our customers may choose to use competitive products, which may be less expensive or may provide faster results than our devices. Clinicians are traditionally slow to adopt new products, testing practices and clinical treatments, partly because of perceived liability risks and the uncertainty of third-party reimbursement. If clinicians, government agencies and hospital administrators do not adopt our products, we may not maintain profitability. Factors that may adversely affect the medical community s acceptance of our products include:

Publication of clinical study results that demonstrate a lack of efficacy or cost-effectiveness of our products;

Changing governmental and physician group guidelines;

Actual or perceived performance, quality, price, and total cost of ownership deficiencies of our products relative to other competitive products;

Our ability to maintain and enhance our existing relationships and to form new relationships with leading physicians, physician organizations, hospitals, state laboratory personnel, and third-party payors;

Changes in state and third-party payor reimbursement policies for our products; and

Repeal of laws requiring universal newborn hearing screening and metabolic screening.

Increased sales through group purchasing organizations and sales to high volume purchasers may reduce our average selling prices, which would reduce our revenue and gross profits

We have entered, and expect in the future to enter into agreements with customers who purchase high volumes of our products. Our agreements with these customers may contain discounts from our normal selling prices and other special pricing considerations, which could cause our revenue and profits to decline. In addition, we have entered into agreements to sell our products to members of GPOs, which negotiate volume purchase prices for medical devices and supplies for member hospitals, group practices and other clinics. While we make sales directly to GPO members, the GPO members receive volume discounts from our normal selling price and may receive other special pricing considerations from us. Sales to members of all GPOs accounted for approximately 24%, 31% and 35% of our total revenue during 2009, 2008 and 2007, respectively, and sales to members of one GPO, Novation LLC, accounted for approximately 8%, 10% and 9% of our total revenue in 2009, 2008 and 2007, respectively. Other of our existing customers may be members of GPOs with which we do not have agreements. Our sales efforts through GPOs may conflict with our direct sales efforts to our existing customers. If we enter into agreements with new GPOs and some of our existing customers begin purchasing our products through those GPOs, our revenue and profits could decline.

Demand for some of our products depends on the capital spending policies of our customers, and changes in these policies could harm our business

A majority of customers for our products are hospitals, physician offices, and clinics. Many factors, including public policy spending provisions, available resources, and economic cycles have a significant effect on the capital spending policies of these entities and therefore the amount that

they can spend on our equipment products. If budget resources limit the capital spending of our customers, they will be unlikely to either purchase any new equipment from us or upgrade to any of our newer equipment products. Lack of liquidity in credit markets and uncertainty about future economic conditions can have an adverse effect on the spending patterns of our customers. These factors can have a significant adverse effect on the demand for our products.

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Our markets are very competitive and in the United States we sell certain of our products in a mature market

We face competition from other companies in all of our product lines. Our competitors range from small, privately-held companies to multinational corporations and their product offerings vary in scope and breadth. We do not believe that any single competitor is dominant in any of our product lines.

The markets for certain of our products in the U.S., including the newborn hearing screening and EEG monitoring markets, are mature and we are unlikely to see significant growth for such products in the U.S. In the U.S. we derive a significant portion of our revenue from the sale of disposable supplies that are used with our hearing screening devices. Because these disposable supply products can generate high margins, we expect that our products, particularly our hearing screening disposable supply products, could face increasing competition, including competitors offering lower prices, which could have an adverse affect on our revenue and margins.

We believe that our primary competitive strengths relate to the functionality and reliability of our products, our recognized brands, and our developed sales channels. Our competitors may have certain competitive advantages, which include the ability to devote greater resources to the development, promotion, and sale of their products. Consequently, we may need to increase our efforts, and related expenses for research and development, marketing, and selling to maintain or improve our position.

We expect recurring sales to our existing customers to generate a majority of our revenue in the future, and if our existing customers do not continue to purchase products from us, our revenue may decline.

Our operating results may decline if we do not succeed in developing, acquiring and marketing additional products or improving our existing products

We intend to develop additional products and technologies, including enhancements of existing products, for the screening, detection, treatment, monitoring and tracking of common medical ailments. Developing new products and improving our existing products to meet the needs of current and future customers requires significant investments in research and development. If we fail to successfully sell new products, update our existing products, or timely react to changes in technology, our operating results may decline as our existing products reach the end of their commercial life cycles.

Our plan to expand our international operations will result in increased costs and is subject to numerous risks; if our efforts are not successful, this could harm our business

We have expanded our international operations through acquisitions and plan to expand our international sales and marketing efforts to increase sales of our products in foreign countries. We may not realize corresponding growth in revenue from growth in international unit sales, due to the lower average selling prices we receive on sales outside of the U.S. Even if we are able to successfully expand our international selling efforts, we cannot be certain that we will be able to create or increase demand for our products outside of the U.S. Our international operations are subject to other risks, which include:

Impact of possible recessions in economies outside the U.S.;

Political and economic instability, including instability related to war and terrorist attacks in the U.S. and abroad;

Contractual provisions governed by foreign law, such as local law rights to sales commissions by terminated distributors;

Decreased healthcare spending by foreign governments that would reduce international demand for our products;

Continued strengthening of the U.S. dollar relative to foreign currencies that could make our products less competitive because approximately half of our international sales are denominated in U.S. dollars;

Greater difficulty in accounts receivable collection and longer collection periods;

Difficulties of staffing and managing foreign operations;

Reduced protection for intellectual property rights in some countries and potentially conflicting intellectual property rights of third parties under the laws of various foreign jurisdictions;

Difficulty in obtaining and maintaining foreign regulatory approval; and

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Attitudes by clinicians, and cost reimbursement policies, towards use of disposable supplies that are potentially unfavorable to our business.

In particular, our international sales could be adversely affected by a strengthening of the U.S. dollar relative to other foreign currencies, which makes our products more costly to international customers for sales denominated in U.S. dollars.

Our operating results may suffer because of our exposure to foreign currency exchange rate fluctuations

Substantially all of our sales contracts with our U.S. based customers provide for payment in U.S. dollars. With the exception of our Canadian operations, substantially all of the revenue and expenses of our foreign subsidiaries are denominated in the applicable foreign currency. To date we have executed only limited foreign currency contracts to hedge these currency risks. Our future revenue and expenses may be subject to volatility due to exchange rate fluctuations that could result in foreign exchange gains and losses associated with foreign currency transactions and the translation of assets and liabilities denominated in foreign currencies.

Substantially all our sales from our U.S. operations to our international distributors also provide for payment in U.S. dollars. A strengthening of the U.S. dollar relative to other foreign currencies could increase the effective cost of our products to our international distributors as their functional currency is typically not the U.S. dollar. This could have a potential adverse effect on our ability to increase or maintain average selling prices of our products to our foreign-based customers.

If guidelines mandating universal newborn hearing screening do not continue to develop in foreign countries and governments do not mandate testing of all newborns as we anticipate, or if those guidelines have a long phase-in period, our sales of newborn hearing screening products may not achieve the revenue growth we have achieved in the past

We estimate that approximately 95% of the children born in the U.S. are currently being tested for hearing impairment prior to discharge from the hospital. To date, there has been only limited adoption of newborn hearing screening prior to hospital discharge by foreign governments, and when newborn hearing screening programs are enacted by foreign governments there can be a phase-in period spanning several years. The widespread adoption of guidelines depends, in part, on our ability to educate foreign government agencies, neonatologists, pediatricians, third-party payors, and hospital administrators about the benefits of universal newborn hearing screening as well as the use of our products to perform the screening and monitoring. Our revenue from our newborn hearing screening product lines may not grow if foreign governments do not require universal newborn hearing screening prior to hospital discharge, if physicians or hospitals are slow to comply with those guidelines, or if governments provide for a lengthy phase-in period for compliance.

Because we rely on distributors or sub-distributors to sell our products in most of our markets outside of the U.S., our revenue could decline if our existing distributors reduce the volume of purchases from us, or if our relationship with any of these distributors is terminated

We currently rely on our distributors or sub-distributors for a majority of our sales outside the U.S. Some distributors also assist us with regulatory approvals and education of clinicians and government agencies. We intend to continue our efforts to increase our sales in Europe, Japan, and other developed countries. If we fail to sell our products through our international distributors, we would experience a decline in revenues unless we begin to sell our products directly in those markets. We cannot be certain that we will be able to attract new international distributors to market our products effectively or provide timely and cost-effective customer support and service. Even if we are successful in selling our products through new distributors, the rate of growth of our revenue could be harmed if our existing distributors do not continue to sell a large dollar volume of our products. None of our existing distributors are obligated to continue selling our products.

We may be subject to foreign laws governing our relationships with our international distributors. These laws may require us to make payments to our distributors if we terminate our relationship for any reason, including for cause. Some countries require termination payments under local law or legislation that may supersede our contractual relationship with the distributor. Any required payments would adversely affect our operating results.

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If we lose our relationship with any supplier of key product components or our relationship with a supplier deteriorates or key components are not available in sufficient quantities, our manufacturing could be delayed and our business could suffer

We contract with third parties for the supply of some of the components used in our products and the production of our disposable products. Some of our suppliers are not obligated to continue to supply us. We have relatively few sources of supply for some of the components used in our products and in some cases we rely entirely on sole-source suppliers. In addition, the lead-time involved in the manufacturing of some of these components can be lengthy and unpredictable. If our suppliers become unwilling or unable to supply us with components meeting our requirements, it might be difficult to establish additional or replacement suppliers in a timely manner, or at all. This would cause our product sales to be disrupted and our revenue and operating results to suffer.

Replacement or alternative sources might not be readily obtainable due to regulatory requirements and other factors applicable to our manufacturing operations. Incorporation of components from a new supplier into our products may require a new or supplemental filing with applicable regulatory authorities and clearance or approval of the filing before we could resume product sales. This process may take a substantial period of time, and we may not be able to obtain the necessary regulatory clearance or approval. This could create supply disruptions that would harm our product sales and operating results.

We depend upon key employees in a competitive market for skilled personnel, and, without additional employees, we cannot grow or maintain profitability

Our products and technologies are complex, and we depend substantially on the continued service of our senior management team. The loss of any of our key employees could adversely affect our business and slow our product development process. Our future success also will depend, in part, on the continued service of our key management personnel, software engineers, and other research and development employees and our ability to identify, hire, and retain additional personnel, including customer service, marketing, and sales staff. Demand for these skilled employees in our industry is very competitive due to the limited number of people available with the necessary technical skills and understanding of our product technologies. We may be unable to attract and retain personnel necessary for the development of our business.

Our ability to market and sell products depends upon receipt of domestic and foreign regulatory approval of our products and manufacturing operations. Our failure to obtain or maintain regulatory approvals and compliance could negatively affect our business

Our products and manufacturing operations are subject to extensive regulation in the United States by the FDA and by similar regulatory agencies in other countries. Our products are classified as medical devices. Medical devices are subject to extensive regulation by the FDA pursuant to regulations that are wide ranging and govern, among other things: design and development; manufacturing and testing; labeling; storage and record keeping; advertising, promotion, marketing, sales distribution and export; and surveillance and reporting of deaths or serious injuries.

Unless an exemption applies, each medical device that we propose to market in the U.S. must first receive one of the following types of FDA premarket review authorizations:

- Clearance via Section 510(k) of the Food, Drug, and Cosmetics Act of 1938, as amended; or
- Premarket approval via Section 515 of the Food, Drug, and Cosmetics Act if the FDA has determined that the medical device in question poses a greater risk of injury.

The FDA will clear marketing of a medical device through the 510(k) process if it is demonstrated that the new product is substantially equivalent to other 510(k)-cleared products. The premarket approval application process is much more costly, lengthy and uncertain than the 510(k) process, and must be supported by extensive data from preclinical studies and human clinical trials. The FDA may not grant either 510(k) clearance or premarket approval for any product we propose to market. Further, any modification to a 510(k)-cleared device that could significantly affect its safety or effectiveness, or that would constitute a major change in its intended use, design or manufacture, requires a new 510(k) clearance or, possibly, approval of a premarket approval application. The FDA requires every manufacturer to make this determination in the first instance, but the FDA may review any manufacturer s decision. If the FDA requires us to seek 510(k) clearance or premarket approval for modification of a previously cleared product for which we have concluded that new clearances or approvals are unnecessary, we may be

required to cease marketing or to recall the modified product until we obtain clearance or approval, and we may be subject to significant regulatory fines or penalties. Further, our products could be subject to recall if the FDA determines, for any reason, that our products are not safe or effective.

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Delays in receipt or failure to receive clearances or approvals, the loss of previously received clearances or approvals, or the failure to comply with existing or future regulatory requirements could adversely impact our operating results. If the FDA finds that we have failed to comply with these requirements, the Agency can institute a wide variety of enforcement actions, ranging from a public warning letter to more severe sanctions such as:

- Fines, injunctions and civil penalties;
- Recall or seizure of our products;
- Issuance of public notices or warnings;
- Imposition of operating restrictions, partial suspension, or total shutdown of production;
- Refusal of our requests for Section 510(k) clearance or premarket approval of new products;
- Withdrawal of Section 510(k) clearance or premarket approvals already granted; or
- Criminal prosecution.

Domestic regulation of our products and manufacturing operations, other than that which is administered by the FDA, includes the Environmental Protection Act, the Occupational Safety and Health Act, and state and local counterparts to these Acts.

Our business would be harmed if the FDA determines that we have failed to comply with applicable regulations governing the manufacture of our products and/or we do not pass an inspection

We and our suppliers are required to demonstrate and maintain compliance with the FDA s Quality System Regulation. The Quality System Regulation sets forth the FDA s requirements for good manufacturing practices of medical devices and includes requirements for, among other things, the design, testing, production processes, controls, quality assurance, labeling, packaging, storage and shipping of such products. In addition, we and our suppliers must engage in extensive recordkeeping and reporting and must make available our manufacturing facility and records for periodic unscheduled inspections by federal, state and foreign agencies, including the FDA. We cannot assure you that we and our suppliers are or will continue to be in full compliance with the Quality System Regulation, and that we will not encounter any manufacturing difficulties.

Failure of our third party suppliers and manufacturers or us to comply with applicable regulations could result in sanctions being imposed on us, including, among other things, fines, injunctions, civil penalties, failure of regulatory authorities to grant marketing approval of our products, delays, suspension or withdrawal of approvals, seizures or recalls of products and manufacturing restrictions, any of which could harm our business.

Our Olympic Cool-Cap product is subject to greater products liability exposure and FDA regulation

The FDA classifies medical devices into one of three classes, depending on the degree of risk associated with each medical device and the extent of controls that are needed to ensure safety and effectiveness. Devices deemed to pose lower risk are placed in either class I or class II. Devices deemed by the FDA to pose the greatest risk, such as life-sustaining, life supporting or implantable devices, or a device deemed to not be substantially equivalent to a previously cleared 510(k) device are placed in class III, and generally require premarket approval from the FDA before they may be marketed.

Our Olympic Cool-Cap is a class III minimally invasive medical device, and as such we may be subject to an increased product liability risk relative to our other class I and class II non-invasive products. In addition, this type of product is subject to greater FDA oversight than our other products and there is greater risk that sales of the product could be interrupted due to the premarket approval processes of the FDA and other regulatory bodies.

Our business may suffer if we are required to revise our labeling or promotional materials, or if the FDA takes an enforcement action against us for off-label uses

We are prohibited by the FDA from promoting or advertising our medical device products for uses not within the scope of our clearances or approvals, or from making unsupported promotional claims about the benefits of our products.

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If the FDA determines that our claims are outside the scope of our clearances, or are unsupported, it could require us to revise our promotional claims or take enforcement action against us. If we were subject to such an action by the FDA, our sales could be delayed, our revenue could decline, and our reputation among clinicians could be harmed. Likewise, if we acquire new products, either through the purchase of products, technology assets, or businesses, that are subsequently deemed to have inadequate supporting data, we may be required to (i) obtain adequate data, which could be costly and impede our ability to market these products, or (ii) modify the labeling on these products, which could impair their marketability, as described above.

If we deliver products with defects, we may incur costs to repair and, possibly, recall that product and market acceptance of our products may decrease.

The manufacturing and marketing of our products involve an inherent risk of our delivering a defective product or products that do not otherwise perform as we expect. We may incur substantial expense to repair any such products and may determine to recall such a product, even if not required to do so under applicable regulations. Any such recall would be time consuming and expensive. Product defects or recalls may adversely affect our customers acceptance of the recalled and other of our products. As an example, in the second quarter of 2010 we discontinued selling the Sonamed Clarity newborn hearing screening product line and incurred costs associated with sales concessions awarded customers who traded in a Clarity device for one our existing newborn hearing screening devices and the write-down of inventory. We also recorded an impairment charge to write-off the carrying value of the Sonamed and Clarity tradenames.

If we fail to comply with healthcare regulations, we could face substantial penalties and our business, operations and financial condition could be adversely affected.

We do not provide healthcare services, control the referral of patients for healthcare services, nor bill Medicare, Medicaid or other third-party payors; however, due to the breadth of many healthcare laws and regulations, we could be subject to healthcare fraud regulation and enforcement by both the federal government and the states in which we conduct our business. The laws that may affect our ability to operate include: (i) the federal healthcare programs Anti-Kickback Law, which prohibits, among other things, persons from knowingly and willfully soliciting, receiving, offering or paying remuneration, directly or indirectly, in exchange for or to induce either the referral of an individual for, or the purchase, order or recommendation of, any good or service for which payment may be made under federal healthcare programs such as Medicare or Medicaid, (ii) federal false claims laws which prohibit, among other things, individuals or entities from knowingly presenting, or causing to be presented, claims for payment from Medicare, Medicaid, or other third-party payors that are false or fraudulent, and which may apply to entities like us which provide coding and billing advice to customers, and/or (iii) state law equivalents of each of the above federal laws, such as anti-kickback and false claims laws which may apply to items or services reimbursed by any third-party payor, including commercial insurers, many of which differ from their federal counterparts in significant ways, thus complicating compliance efforts.

If our operations are found to be in violation of any of the laws described above or any other governmental regulations that apply to us, we may be subject to penalties, including civil and criminal penalties, damages, fines and the curtailment or restructuring of our operations. Any penalties, damages, fines, curtailment or restructuring of our operations could adversely affect our ability to operate our business and our financial results. The risk of our being found in violation of these laws is increased by the fact that their provisions are open to a variety of interpretations. Any action against us for violation of these laws, even if we successfully defend against it, could cause us to incur significant legal expenses and divert our management s attention from the operation of our business.

Our operating results would suffer if we were subject to a protracted infringement claim

The medical technology industry is characterized by a substantial amount of litigation and related administrative proceedings regarding patents and intellectual property rights. We expect that medical screening and diagnostic products may become increasingly subject to third-party infringement claims as the number of competitors in our industry grows and the functionality of products overlap. Third parties such as individuals, educational institutions or other medical device companies may claim that we infringe their intellectual property rights. Any claims, with or without merit, could have any of the following negative consequences:

Result in costly litigation and damage awards;

Divert our management s attention and resources;

Cause product shipment delays or suspensions; or

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Require us to seek to enter into royalty or licensing agreements.

A successful claim of infringement against us could result in a substantial damage award and materially harm our financial condition. Our failure or inability to license the infringed or similar technology, or design and build non-infringing products, could prevent us from selling our products and adversely affect our business and financial results.

We may also find it necessary to bring infringement actions against third parties to seek to protect our intellectual property rights. Litigation of this nature, even if successful, is often expensive and disruptive of our management s attention, and in any event may not lead to a successful result relative to the resources dedicated to any such litigation.

We license intellectual property rights from third parties and would be adversely affected if our licensors do not appropriately defend their proprietary rights or if we breach any of the agreements under which we license commercialization rights to products or technology from others

We license rights from third parties for products and technology that are important to our business. If our licensors are unsuccessful in asserting and defending their proprietary rights, including patent rights and trade secrets, we may lose the competitive advantages we have through selling products that we license from third parties. Additionally, if it is found that our licensors infringe on the proprietary rights of others, we may be prohibited from marketing our existing products that incorporate those proprietary rights. Under our licenses, we are subject to commercialization and development, sublicensing, royalty, insurance and other obligations. If we fail to comply with any of these requirements, or otherwise breach a license agreement, the licensor may have the right to terminate the license in whole or to terminate the exclusive nature of the license.

Product liability suits against us could result in expensive and time consuming litigation, payment of substantial damages, and an increase in our insurance rates

The sale and use of our products could lead to the filing of a product liability claim by someone claiming to have been injured using one of our products or claiming that one of our products failed to perform properly. A product liability claim could result in substantial damages and be costly and time consuming to defend, either of which could materially harm our business reputation or financial condition. Our product liability insurance may not protect our assets from the financial impact of defending a product liability claim. Any product liability claim brought against us, with or without merit, could increase our product liability insurance rates or prevent us from securing any coverage in the future.

We have experienced seasonality in the sale of our products

We experience seasonality in our revenue. For example, our sales typically decline from our fourth fiscal quarter to our first fiscal quarter, due to patterns in the capital budgeting and purchasing cycles of our current and prospective customers, many of which are government agencies, and the compensation arrangements of our direct sales employees, as those arrangements are tied to calendar-year sales plans. We may also experience declining sales in the third fiscal quarter due to summer holiday and vacation schedules. We anticipate that we will continue to experience these seasonal fluctuations, which may lead to fluctuations in our quarterly operating results. We believe that you should not rely on our results of operations for interim periods as an indication of our expected results in any future period.

ITEM 6. Exhibits

(a) Exhibits

		Incorporated By Reference			
		Exhibit			
Exhibit No.	**Exhibit**	**Filing**	**No.**	**File No.**	**File Date**
31.1					

	Certification of Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification of Principal Executive Officer and Principal Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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SIGNATURES

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 thereunto duly authorized.

NATUS MEDICAL INCORPORATED

Dated: November 5, 2010 By: /s/ JAMES B. HAWKINS
James B. Hawkins

President and Chief Executive Officer

(Principal Executive Officer)

Dated: November 5, 2010 By: /s/ STEVEN J. MURPHY
Steven J. Murphy

Vice President Finance and

Chief Financial Officer

(Principal Financial and

Accounting Officer)

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NATUS MEDICAL INCORPORATED

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