

ATC Ventures Group, Inc.
Form 10-Q/A
April 16, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q/A

(Mark one)

- QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934.

For the quarterly period ended March 31, 2011

OR

- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE EXCHANGE ACT OF 1934.

For the transition period from to
Commission file number: 001-31715

Cycle Country Accessories Corp.

(Exact name of registrant as specified in its charter)
Nevada

(State or other jurisdiction of incorporation or organization)
42-1523809

(IRS Employer Identification No.)

1701 38th Ave W, Spencer, Iowa 51301

(Address of principal executive offices)

P: (712) 262-4191

F: (712) 262-0248

www.cyclecountry.com

(Registrant's telephone number, facsimile number, and corporate website)

Check whether the issuer (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes 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 (Section 232.405 of this chapter) during the preceding 12 months (or 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 definition of "large accelerated filer" and "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No
The number of shares of the registrant's common stock, par value \$0.0001 per share, outstanding as of May 23, 2011 is 6,990,662

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EXPLANATORY NOTE

We are filing this Amended Quarterly Report on Form 10-Q/A (the "Amended Filing") to our Quarterly Report on Form 10-Q/A for the fiscal quarter ended March 31, 2011 (the "Original Filing"), to correct errors relating to the number of shares outstanding, the valuation and timing of the expense recognition of employee equity awards, and the amount, timing and income statement classification of sales discounts, allowances and expenses related to a customer incentive program that was put into place by former management and the error regarding the number of shares outstanding related to equity compensation awards with multiple vesting dates that covered multi-year service periods. These errors, in total, caused us to understate total revenue and overstate selling expenses related to our customer incentive program, while understating our stock-based compensation expense. Additionally, the error regarding the number of shares that were to have been issued and outstanding had the effect of further misstating the basic and fully-diluted earnings per share for the three and six months ended March 31, 2011. The effects of these restatements are disclosed in Note 11- Restatement of Consolidated Financial Statements.

No other changes are being made other than the updating of: (i) the Exhibits to include updated Certifications of the Chief Executive and Chief Financial Officers, and (ii) the Exhibit Index to disclose that certain exhibits that were filed with the Original Filing are incorporated by reference into this Amended Filing. The sections of the Original Filing that are not being amended are unchanged and continue in full force and effect as originally filed. This Amended Filing speaks as of the date of the Original Filing and has not been updated to reflect events occurring subsequent to the date of the Original Filing.

Part I Financial Information

Item 1. Financial Statements

Cycle Country Accessories Corp. and Subsidiaries Condensed Consolidated Balance Sheet

	March 31, 2011 (Restated)(1) (Unaudited)	September 30, 2010 (Restated)(1)
Assets		
Current Assets		
Cash and cash equivalents	\$ 147,830	\$ 28,939
Accounts receivable, net	340,028	1,879,491
Inventories	2,236,560	2,716,639
Income taxes receivable	627,434	640,733
Deferred income taxes	517,000	366,000
Prepaid expenses and other	237,696	320,475
Assets held for sale	189,250	795,439
Total current assets	4,295,798	6,747,716
Property, plant and equipment, net	9,609,782	9,809,351
Intangible assets, net	50,385	161,957
Other assets	3,387	7,413
Total assets	\$ 13,959,352	\$ 16,726,437
Liabilities and Stockholders' Equity		
Current Liabilities		
Disbursements in excess of bank balances	\$ 238,826	\$ 387,141
Accounts payable	1,769,570	689,030
Accrued expenses	1,355,847	1,049,385
Bank line of credit	1,528,305	2,700,000
Current portion of notes payable	465,829	699,681
Liabilities related to assets held for sale	24,995	12,409
Current portion of deferred gain	-	27,754
Total current liabilities	5,383,372	5,565,400
Long-Term Liabilities		
Notes payable, less current portion	2,261,018	2,478,279
Deferred income taxes	918,000	1,587,000

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Total long term liabilities	3,179,018	4,065,279
Total liabilities	8,562,390	9,630,679

Stockholders' Equity

Common stock, \$.0001 par value; 100,000,000 shares authorized; 6,990,662 (Restated) and 8,046,471 shares issued and outstanding, respectively	699	805
Additional paid-in capital	12,458,017	12,495,917
Accumulated deficit	(7,061,754)	(5,400,964)
Total stockholders' equity	5,396,962	7,095,758

Total liabilities and stockholders' equity	\$	13,959,352	\$	12,726,437
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(1)See Note 11- Restatement of Consolidated Financial Statements- of Notes to Condensed Consolidated Financial Statements

See accompanying notes to the unaudited condensed consolidated financial statements.

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Cycle Country Accessories Corp. and Subsidiaries
Condensed Consolidated Statements of Operations

	Three Months ended March 31,	
	2011 (Restated)(1) (Unaudited)	2010 (Unaudited)
Revenue		
Net sales	\$ 2,820,384	\$ 2,159,994
Freight income	35,526	27,389
Total revenues	2,855,910	2,187,383
Cost of goods sold		
Cost of goods sold	2,548,828	1,455,739
Lower of cost or market adjustment	480,918	-
Gross profit (loss)	(173,836)	731,644
Selling, general, and administrative expenses		
Selling, general, and administrative expenses	1,429,739	1,005,343
Fraud expense	-	134,775
Total operating expenses	1,429,739	1,140,118
Loss from operations	(1,603,575)	(408,474)
Other income (expense)		
Interest expense	(73,567)	(70,856)
Interest income	-	1
Miscellaneous	60,171	46,543
Total other expense, net	(13,396)	(24,312)
Loss from continuing operations before income tax benefit	(1,616,971)	(432,786)
Benefit from income taxes	534,394	172,742
Net loss from continuing operations	(1,082,577)	(260,044)
Loss from discontinued operations, net of tax	(269,134)	(28,427)
Net loss	\$ (1,351,711)	\$ (288,471)
Weighted average shares of common stock:		
Basic	6,990,662	5,992,919
Diluted	6,990,662	5,992,919
Loss per basic and diluted share:		
Continuing Operations	\$ (0.15)	\$ (0.04)
Discontinued Operations	\$ (0.04)	\$ -

(1) See Note 11- Restatement of Consolidated Financial Statements- of Notes to Condensed Consolidated Financial Statements

See accompanying notes to the unaudited condensed consolidated financial statements.

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Cycle Country Accessories Corp. and Subsidiaries
Condensed Consolidated Statements of Operations

	Six Months ended March 31,	
	2011 (Restated)(1) (Unaudited)	2010 (Unaudited)
Revenue		
Net sales	\$ 6,933,110	\$ 6,190,909
Freight income	57,307	50,482
Total revenues	6,990,417	6,241,391
Cost of goods sold		
Cost of goods sold	5,906,255	4,218,484
Lower of cost or market adjustment	480,918	-
Gross profit	603,245	2,022,907
Selling, general, and administrative expenses		
Selling, general, and administrative expenses	2,546,550	1,854,964
Fraud expense	-	134,775
Total operating expenses	2,546,550	1,989,739
Income (loss) from operations	(1,943,305)	33,168
Other income (expense)		
Interest expense	(172,316)	(153,245)
Interest income	-	3
Miscellaneous	87,246	81,031
Total other expense, net	(85,070)	(72,211)
Loss from continuing operations before income tax benefit	(2,028,375)	(39,043)
Benefit from income taxes	665,022	20,385
Net loss from continuing operations	(1,363,353)	(18,658)
Loss from discontinued operations, net of tax	(297,437)	(42,536)
Net loss	\$ (1,660,790)	\$ (61,194)
Weighted average shares of common stock:		
Basic	7,518,567	6,033,224
Diluted	7,518,567	6,033,224
Loss per basic and diluted share:		
Continuing Operations	\$ (0.18)	\$ -
Discontinued Operations	\$ (0.04)	\$ (0.01)

(1) See Note 11- Restatement of Consolidated Financial Statements- of Notes to Condensed Consolidated Financial Statements

See accompanying notes to the unaudited condensed consolidated financial statements.

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Cycle Country Accessories Corp. and Subsidiaries
Condensed Consolidated Statements of Cash Flows

	Six Months ended March 31,	
	2011 (Restated)(1) (Unaudited)	2010 (Unaudited)
Cash Flows from Operating Activities from Continuing Operations:		
Net loss from continuing operations	\$ (1,363,353)	\$ (18,658)
Adjustments to reconcile net loss from continuing operations to net cash provided by operating activities:		
Depreciation	309,885	352,608
Amortization	779	673
Reserve for bad debts	60,000	-
Lower of cost or market adjustment	480,918	-
Stock-based compensation	87,627	13,750
Loss on sale of property, plant and equipment	13,319	114,112
Deferred income taxes	(820,000)	-
Fraud recovery	-	(120,000)
Change in operating assets and liabilities:		
Accounts receivable	1,479,463	1,153,953
Inventories	(840)	166,641
Income tax receivable	13,299	5,546
Prepaid expenses, net	82,779	(8,189)
Other assets	4,026	3,988
Accounts payable, net	1,080,540	(215,291)
Accrued expenses	177,718	(119,635)
Net cash provided by operating activities from continuing operations	1,606,159	1,329,498
Cash Flows from Investing Activities from Continuing Operations		
Purchase of property, plant and equipment	(76,909)	(164,477)
Purchase of intangible assets, net	(1,755)	(2,660)
Proceeds from sale of property, plant and equipment	5,338	12,500
Net cash used for investing activities in continuing operations	(73,326)	(154,637)
Cash Flows from Financing Activities from Continuing Operations:		
Disbursements in excess of bank balances	(148,315)	(438,636)
Payments on bank notes payable	(451,113)	(423,247)
Bank line of credit, net	(1,171,695)	(288,164)
Net cash used for financing activities from continuing operations	(1,771,123)	(1,150,047)
Cash Flows from Discontinued Operations:		
Cash provided by operating activities	357,181	14,443
Net cash provided by discontinued operations	357,181	14,443
Net increase in cash and cash equivalents	118,891	39,257
Cash and cash equivalents, beginning of period	28,939	27,490

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Cash and cash equivalents, end of period	\$	147,830	\$	66,747
(1)See Note 11- Restatement of Consolidated Financial Statements- of Notes to Condensed Consolidated Financial Statements				

See accompanying notes to the unaudited condensed consolidated financial statements.

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Cycle Country Accessories Corp. and Subsidiaries
Condensed Consolidated Statements of Cash Flow

	Six Months ended March 31,	
	2011 Restated(1) (Unaudited)	2010 (Unaudited)
Supplemental disclosures of cash flow information:		
Cash paid during the period for:		
Interest	\$ 174,786	\$ 153,000
Supplemental schedule of non-cash investing and financing:		
Treasury stock purchased included in accrued expense	\$ 128,744	\$ -
Disposal of fixed assets	\$ 56,131	\$ -

(1) See Note 11- Restatement of Consolidated Financial Statements- of Notes to Condensed Consolidated Financial Statements

See accompanying notes to the unaudited condensed consolidated financial statements.

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Cycle Country Accessories Corp Notes to Condensed Consolidated Financial Statements (Unaudited)

Note 1. Summary of Significant Accounting Policies:

Basis of Presentation - The accompanying unaudited condensed consolidated financial statements for the three months and six months ended March 31, 2011 and 2010 have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission for Form 10-Q/A. Accordingly, they do not include all the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. It is the opinion of management that the accompanying unaudited condensed consolidated financial statements contain all adjustments, consisting only of normal recurring accruals, considered necessary for a fair presentation of the Company's financial position, results of operations, and cash flows for the periods presented.

The results of operations for the interim periods ended March 31, 2011 and 2010 are not necessarily indicative of the results to be expected for the full year. These interim condensed consolidated financial statements should be read in conjunction with the September 30, 2010 consolidated financial statements and related notes included in the Company's Annual Report on Form 10-K/A for the fiscal year ended September 30, 2010.

Reporting Entity and Principles of Consolidation - Cycle Country Accessories Corp. ("Cycle Country") a Nevada corporation, has a wholly-owned subsidiary, Cycle Country Accessories Corp. ("Cycle Country - Iowa"), an Iowa corporation.

The entities are collectively referred to as the "Company" for these condensed consolidated financial statements. All significant intercompany balances and transactions have been eliminated in consolidation.

Nature of the Business - The Company has two distinct segments engaged in the design, manufacture, sale and distribution of products. One of the segments has branded, proprietary products, and the other is a contract manufacturing division. The largest segment, Cycle Country ATV Accessories, designs, manufactures and sells a popular selection of branded accessories for vehicles in the Powersports industry which are sold to various wholesale distributors and retail dealers throughout the United States of America, Canada, Mexico, South America, Europe, and Asia. Imdyne is engaged in the design, manufacture and assembly of an array of parts for original equipment manufacturers (OEMs) and other customers. The Company has offices in Minnetonka, MN and Spencer, IA, and has approximately 160,000 square feet of modern manufacturing facilities including its owned building in Spencer and leased space in Milford, IA.

The Company records assets, liabilities, revenues and expenses associated with two other segments as discontinued operations for all periods presented. Plazco manufactures, sells, and distributes injection-molded plastic products for vehicles such as golf cars, and low-speed vehicles (LSVs). Perf-Form manufactures, sells, and distributes oil filters for the Powersports industry, including ATVs, UTVs and Motorcycles. As more fully disclosed in Note 9, during the three months ended March 31, 2011 the Company has concluded that these segments do not fit within the long-term strategic plans of the Company.

Revenue Recognition - The Company primarily ships products to its customers by third party carriers. The Company recognizes revenues from product sales when title and risk of loss to the products is passed to the customer, which occurs at the point of shipping.

Certain costs associated with the shipping and handling of products to customers are billed to the customer and included as freight income in the accompanying condensed consolidated statements of operations. The actual freight costs incurred are included in cost of goods sold. Sales were recorded net of sales discounts, returns and allowances. Sales discounts and allowances were approximately \$321,000 (restated) and \$36,000 for the three months ended March 31, 2011 and 2010, respectively. For the six months ended March 31, 2011 and 2010 respectively, sales discounts and allowances were approximately \$485,000 (restated) and \$354,000. Of these amounts, discounts and allowances related to continuing operations were approximately \$293,000 (restated) and \$33,000 for the three months ended March 31, 2011 and 2010 respectively and \$478,000 (restated) and \$348,000 for the six months ended March 31, 2011 and 2010, respectively.

Cost of Goods Sold - The components of cost of goods sold in the accompanying condensed consolidated statements of operations include overhead allocation, all direct materials and direct labor associated with the assembly and/or manufacturing of the Company's products.

Cash and Cash Equivalents - The Company considers all highly liquid investments with an original maturity of three months or less to be cash equivalents. The Company maintains its accounts primarily at one financial institution. At times throughout the year, the Company's cash and cash equivalent balances may exceed amounts insured by the Federal Deposit Insurance Company.

Accounts Receivable - Credit terms are generally extended to customers on a short-term basis. These receivables do not bear interest, although a finance charge may be applied to balances more than thirty days past due. Trade accounts receivable are carried on the books at their net realizable value. The Company performs ongoing credit evaluations of its customers to reduce credit risk.

Individual trade accounts receivable are periodically evaluated for collectability based on past credit history and their current financial condition. Trade accounts receivable are charged against the allowance for doubtful accounts when such receivables are deemed to be uncollectible. While the Company has a large customer base that is geographically dispersed, a slowdown in markets in which the Company operates may result in higher than expected uncollectible accounts, and therefore, the need to revise estimates for bad debts. To the extent historical experience is not indicative of future performance or other assumptions used by management do not prevail, the provision for uncollectible accounts could differ significantly, resulting in either higher or lower future provisions for uncollectible accounts. The allowance for doubtful accounts was \$75,000 and \$15,000 at March 31, 2011 and September 30, 2010, respectively. It is at least reasonably possible that the Company's estimate will change in the future.

Inventories - Inventory is stated at the lower of cost or market. Inventory consists of raw material, work in process, and finished goods. Cost is determined using the weighted average method.

Property, Plant, and Equipment - Property, plant and equipment is stated at cost. Depreciation is provided over the estimated useful lives of the assets by using the straight-line and accelerated methods. Long-lived assets, such as property, plant, and equipment, are reviewed for possible impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The Company determined that indicators of potential impairment existed because the Company experienced a decrease in the Company's market capitalization for a sustained period of time. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows (undiscounted and without interest charges) expected to be generated by the asset. If these projected cash flows are less than the carrying amount, impairment is recognized to the extent that the carrying value exceeds its fair value. Fair value is determined through various valuation techniques, including discounted cash flow models, quoted market values and third party appraisals, as considered necessary. In accordance with Accounting Standards Codification, "ASC" 360, the Company evaluated its long-lived assets using an undiscounted cash flow analysis. This analysis supported the carrying value of the long-lived assets and, therefore, no impairment was recorded. The Company's analysis uses significant estimates in its evaluation. It is reasonably possible that its estimates and assumptions could change in the near future, which could lead to further impairment of long-lived assets. The estimated useful lives are as follows:

Asset Description	Years
Land Improvements	15-20
Building	15-40
Plant Equipment	7-10
Tooling and Dies	3-7
Vehicles	3-7
Office Equipment	3-10

Maintenance and repairs are expensed as incurred; major improvements and betterments are capitalized.

Intangible Assets - Intangible assets with estimable useful lives are amortized over their respective estimated useful lives. Intangible assets are reviewed for possible impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

As discussed more fully in Note 9, the Company concluded that the Perf-Form and Plazco segments may not fit within the long-term strategic plans for the Company. As such, the Company determined that indicators of potential impairment existed in the value of trademarks and patents for its Perf-Form segment. Plazco's intangible assets had been previously fully amortized. Recoverability of intangible assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows (undiscounted and without interest charges) expected to be generated by the asset. If these projected cash flows are less than the carrying amount, impairment is recognized to the extent that the carrying value exceeds its fair value. Fair value is determined through various valuation techniques, including discounted cash flow models, quoted or estimated market values and third party appraisals, as considered necessary. This analysis did not support the carrying value of the intangible assets for the Perf-Form segment and, therefore, an impairment charge in the amount of \$100,000 for trademarks and \$10,186 for unamortized

patents was recognized in the three months ended March 31, 2011. These charges are included in discontinued operations.

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Warranty Costs - Estimated future costs related to product warranties are accrued as products are sold based on prior experience and known current events and are included in accrued expenses in the accompanying condensed consolidated balance sheets. Accrued warranty costs have historically been sufficient to cover actual costs incurred.

Income Taxes - Income taxes are provided for the tax effects of transactions reported in the condensed consolidated financial statements and consist of taxes currently receivable and deferred taxes related primarily to differences between the basis for financial and income tax reporting. Deferred taxes also are recognized for operating losses that are available to offset future taxable income and tax credits that are available to offset future income taxes payable. The Company follows a two-step approach to recognizing and measuring tax benefits and liabilities when realization of the tax position is uncertain. The first step is to determine whether the tax positions meet the more-likely-than-not condition for recognition and the second step is to determine the amount to be recognized based on the cumulative probability that exceeds 50%.

The Company recognizes in its condensed consolidated financial statements only those tax positions that are "more-likely-than-not" of being sustained upon examination by taxing authorities, based on the technical merits of the position.

The Company files income tax returns in the U.S. federal jurisdiction and various state jurisdictions. With a few exceptions, the Company is no longer subject to U.S. federal, state, or local income tax examinations by tax authorities for years before 2008. The Company's policy is to recognize interest and penalties related to uncertain tax benefits in income tax expense. The Company has no significant accrued interest or penalties related to uncertain tax positions as of October 1, 2010 or March 31, 2011 and such uncertain tax positions as of each reporting date are insignificant.

Stock-Based Compensation - The Company accounts for stock-based compensation on a fair value basis. The estimated grant date fair value of each stock-based award is recognized in expense over the requisite service period (generally the vesting period). Non-vested stock awards are recorded as compensation expense over the requisite service periods based on the market value on the date of grant.

Earnings (Loss) Per Share - Basic earnings (loss) per share ("EPS") is calculated by dividing net income (loss) by the weighted-average number of shares outstanding during the period. Diluted EPS is computed in a manner consistent with that of basic EPS while giving effect to the potential dilution that could occur if stock options or other share-based awards were exercised, by dividing net income (loss) by the weighted average number of shares and share equivalents during the period. See Note 6 for details regarding basic and diluted earnings per share.

Legal - The Company is subject to legal proceedings and claims which arise in the ordinary course of its business. While the ultimate outcome of these matters is not presently determinable, it is in the opinion of management that the resolution of outstanding claims will not have a material adverse effect on the financial position or results of operations of the Company. Due to the uncertainties in the settlement process, it is at least reasonably possible that management's view of outcomes will change in the near term.

Advertising - Advertising consists primarily of trade magazine advertisements, product brochures and catalogs, and trade shows. Advertising expense totaled approximately \$52,000 and \$31,000 for the three months ended March 31, 2011 and 2010 respectively and \$87,000 and \$65,000 in the six month period ended March 31, 2011 and 2010 respectively, and is included in selling, general, and administrative expenses in the accompanying condensed consolidated statements of operations.

Research and Development Costs - Research and development costs are expensed as incurred. Research and development costs totaled approximately \$117,000 (restated) and \$91,000 in the three month period ended March 31, 2011 and 2010, respectively, and totaled approximately \$211,000 (restated) and \$177,000 for the six months ended March 31, 2011 and 2010 respectively and are included in selling, general and administrative expenses and cost of goods sold in the accompanying condensed consolidated statements of operations.

Shipping and Handling Costs - Shipping and handling costs represent costs associated with shipping products to customers and handling finished goods. Shipping and handling costs totaled approximately \$56,000 and \$67,000 in the three months ended March 31, 2011 and 2010, respectively and totaled approximately \$120,000 and \$135,000 in the six months ended March 31, 2011 and 2010, respectively, and are included in cost of goods sold in the accompanying condensed consolidated statements of operations.

Use of Estimates - The preparation of condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, and operating results, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses. Significant items subject to such estimates include the useful lives and assumptions used in the impairment analysis of long-lived assets; valuation of deferred tax assets; allowance for doubtful accounts; and allowance for inventory

reserves. Actual results could differ significantly from those estimates.

Fair Value of Financial Instruments - The Company utilizes Financial Accounting Standards Board ASC 820 "Fair Value Measurements" which defines fair value, outlines a framework for measuring fair value (although it does not expand the required use of fair value) and details the required disclosures about fair value measurements. At March 31, 2011, the Company does not have any financial or nonfinancial assets or liabilities that would require fair value recognition or disclosures under ASC 820.

The Company estimates that the fair value of all financial instruments at March 31, 2011 approximates their carrying values in the accompanying balance sheet. The estimated fair value amounts have been determined by the Company using appropriate valuation methodologies. As a result of its analysis of intangible assets, the Company reduced the book value of intangible assets related to the Perf-Form segment to \$0 during the three months ended March 31, 2011. The impairment charge of approximately \$110,000 is included in the loss from discontinued operations.

Note 2. Misappropriation of Funds

The Company previously reported the misappropriation of funds by its then-Chairman of the Board of Directors and its Audit Committee, Mr. L. G. Hancher Jr. in the fiscal year ended September 30, 2009. This misappropriation of funds was related to a plan for the Company to purchase shares of its own stock which was to be completed by Mr. Hancher on the Company's behalf (the "Stock Buyback") in fiscal 2009. The Company continues to work to recover all of the amounts misappropriated. During the year ended September 30, 2010, the Company recovered and cancelled 195,416 shares of Company stock with a market value of \$120,000, which reduced common equity and was recorded against fraud expense, net in the consolidated statement of operations. The Company believes the value represents the amount the Company provided for the purchase of shares to the third party that returned these shares to the Company. The price per share is consistent with the trading in the market at the time the Company believed that the shares were being purchased on its behalf.

In June 2010, the Company commenced a lawsuit against Mr. Hancher. On August 2, 2010, Mr. Hancher filed a Chapter 7 petition in the Bankruptcy Court for the Southern District of Indiana. Proceedings in the Bankruptcy Court are pending. There has been no recovery to date on this action and the amount of a potential recovery, if any, cannot be reasonably estimated at this time.

On January 13, 2011, the Securities and Exchange Commission filed a complaint in U.S. District Court, Northern District of Iowa, against Mr. Hancher and various affiliates of his, charging them with six counts of securities violations involving multiple issuers, including the Company. On the same day, Mr. Hancher entered into a consent agreement with the SEC in which, among other things, Mr. Hancher agreed to pay back an aggregate of approximately \$2.4 million in disgorgement, plus approximately \$600,000 in pre-judgment interest, and a fine of \$130,000.

On May 18, 2011, the Securities and Exchange Commission issued an Order Instituting Administrative Proceedings Pursuant to Section 15(b) of the Securities Exchange Act of 1934, Making Findings and Imposing Remedial Sanctions against Mr. Hancher. The order bars Mr. Hancher from associating with any broker, dealer, etc., and while he consented to the entry of the permanent injunction against him, he did so without admitting or denying any the findings of the Order.

At this time, it is not believed that this will result in restitution to the Company in the foreseeable future, based on the previous filings in Mr. Hancher's pending bankruptcy case.

Additional recoveries, if any, will impact subsequent periods and will be reported for the periods in which such recoveries occur. The possibility of any future recoveries and the amount of any such recovery remain uncertain, and the Company can have no assurance that any such recoveries can be achieved or that they can be achieved without significant cost to the Company.

Note 3. Inventories:

Inventories are stated at the lower of cost or market using the weighted average cost method. Cost includes materials, labor, and manufacturing overhead related to the purchase and production of inventories. Management regularly reviews inventory quantities on hand, future product demand, and the estimated utility of inventory. If the review indicates a deduction in utility below carrying value, management would reduce the Company's inventory to a new cost basis through a lower of cost or market adjustment.

Though we routinely do this analysis each quarter, as discussed more fully in the Executive-level Overview of Item 2, Management Discussion and Analysis, the recent changes in our senior sales, marketing, and product development management allowed us to analyze the inventory from a fresh perspective. This evaluation concluded that the need existed to more aggressively challenge the prior sales and marketing team's processes and conclusions.

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During the three months ended March 31, 2011, management evaluated the carrying amount of inventory as it compared to the market values. As a result of the evaluation, the Company recorded an adjustment to inventory in the amount of \$480,918. This charge is recorded in the condensed consolidated financial statements as a lower of cost or market adjustment. During the same period, the company adjusted inventory held in the segments identified as discontinued operations to lower of cost or market, as well. This adjustment totaled \$223,134 and is included in the net loss from discontinued operations. For the three month period ending March 31, 2011, these two adjustments to inventory totaled \$704,052.

The major components of inventories are as follows:

	March 31, 2011 (Unaudited)	September 30, 2010
Raw Material	\$ 665,393	\$ 895,688
Work in Process	86,908	68,631
Finished Goods	1,634,259	1,902,320
Inventory Reserve	(150,000)	(150,000)
Total Inventories	\$ 2,236,560	\$ 2,716,639

Management has evaluated the Company's inventory reserve based on historical experience and current economic conditions and determined that, after the adjustments of lower of cost or market noted above, an inventory reserve of approximately \$150,000 at March 31, 2011 and September 30, 2010 remains appropriate. It is reasonably possible the inventory reserve will change in the near future.

Note 4. Line of Credit:

The Company has a line of credit ("Line of Credit One") for the lesser of \$1,000,000 or 80% of eligible accounts receivable and 35% of eligible inventory. Line of Credit One bears interest at prime (3.25% at March 31, 2011 and September 30, 2010) plus 0.50% with a ceiling of 10.5% and a floor of 6.5%. At March 31, 2011 and September 30, 2010, the rate was 6.5%. At March 31, 2011 and September 30, 2010 there was \$1,000,000 due on Line of Credit One.

On September 30, 2009, the Company and its commercial lender entered into an additional secured credit agreement, ("Line of Credit Two"), dated September 30, 2009, as a temporary expansion of its credit facility Under the terms of Line of Credit Two, the Company added an additional line of credit for the lesser of \$500,000 or 80% of eligible accounts receivable and 35% of eligible inventory. The line was subsequently increased to \$600,000. The interest rate on Line of Credit Two was at 6.5%. There was no amount due on Line of Credit Two at March 31, 2011 or September 30, 2010.

On July 16, 2010, the Company entered into an agreement with its commercial lender to replace Line of Credit Two with a new, larger facility, ("Line of Credit Three"). Under the terms of Line of Credit Three, the Company has added an additional line of credit for the lesser of \$1,700,000 or 80% of eligible accounts receivable and 35% of inventory and bears interest at 6.75%. The note is collateralized by all of the Company's assets. The balance of Line of Credit Three was \$528,305 and \$1,700,000 as of March 31, 2011 and September 30, 2010, respectively.

Lines of Credit One, Two and Three contain conditions and covenants that prevent or restrict the Company from engaging in certain transactions without the consent of the commercial lender and require the Company to maintain certain financial ratios, including term debt coverage and maximum leverage. In addition, the Company is required to maintain a minimum working capital and shall not declare or pay any dividends or any other distributions without the consent of the lender. As more fully described in Note 5, as of and for the three months and six months ending March 31, 2011, the Company was not in compliance with all of its covenants with the lender.

As of January 17, 2011, the Company and its lender entered into the Seventh Amendment to the Secured Credit Agreement and Waiver ("Amendment 7"). Amendment 7 replaces Line of Credit One, Line of Credit Two and Line of Credit Three with a Revolving Credit Agreement in an amount not to exceed \$2,700,000, maturing on March 31, 2011.

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As of March 30, 2011, the Company and its lender entered into the Eighth Amendment to the Secured Credit Agreement and Waiver ("Amendment 8"). Amendment 8 replaces Amendment 7 with a Revolving Credit Agreement in an amount not to exceed \$2,000,000, maturing on June 1, 2011.

Note 5. Long-Term Debt

Long term debt consists of the following:

	March 31, 2011 (Unaudited)	September 30, 2010
Note 1 to commercial lender payable in equal monthly installments of \$42,049 including interest at 6.125%. The note matured April 2011.	\$ 37,519	\$ 284,263
Note 2 to commercial lender payable in equal monthly installments of \$33,449 including interest fixed at 6.125% until April 2011. Beginning April 2011, the interest is reset every 60 months to 0.50% over prime not to exceed 10.5% or be less than 5.5%. The note matures April 2018 and is secured by all Company assets.	2,289,874	2,418,530
Note 3 to commercial lender payable in equal monthly installments of \$14,567 including interest at 6.125% until maturity of April 2013 secured by the specific equipment acquired.	339,454	415,167
Note due to Spencer Area Jobs Trust, due in full March 2014 interest free and forgivable in full if the Company maintains required job levels.	60,000	60,000
Total	2,726,847	3,177,960
Less current maturities	(465,829)	(699,681)
Net	\$ 2,261,018	\$ 2,478,279

These secured credit agreements contain conditions and covenants that prevent or restrict the Company from engaging in certain transactions without the consent of the commercial lender and require the Company to maintain certain financial ratios, including term debt coverage and maximum leverage. As of and for the three and six months ended March 31, 2011, the Company was not in compliance with the term debt coverage requirement or the working capital requirement of the agreement.

As of January 17, 2011, the Company and its lender entered into Amendment 7. Under the terms of Amendment 7, the lender agreed to waive the noncompliance by the Company with the required ratio of current assets to current liabilities as of September 30, 2010, December 31, 2010 and the Company's anticipated noncompliance with the required ratio of current assets to current liabilities through October 1, 2011 and further, waive the Company's noncompliance with the Term Debt Coverage Ratio as of September 30, 2010, December 31, 2010, and the Company's anticipated noncompliance with the Term Debt Coverage Ratio through October 1, 2011.

On April 29, 2010, the Company entered into an agreement with the Spencer Area Jobs Trust (the "Trust"). Under the terms of this agreement, the Trust advanced \$60,000 to the Company under a loan which is forgivable if the Company maintains no less than seventy full time employment positions through February 2014. If the Company does not maintain seventy employment positions, the amount of the loan forgiven will equal \$850 for each employment position retained. The Company will extinguish this debt amount, if any, upon notice from the Trust.

Note 6. Earnings (Loss) Per Share:

Basic earnings (loss) per share is computed by dividing net income (loss) by the weighted average number of shares outstanding during the period. Diluted earnings (loss) per share is computed by dividing net income (loss) by the weighted average number of shares and share equivalents outstanding during the period.

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The Company incurred a net loss of \$1,351,711 (restated) for the three months ended March 31, 2011 and \$1,660,790 (restated) for the six months ended March 31, 2011. A net loss causes all outstanding common stock equivalents, such as certain stock options and warrants, to be antidilutive. As a result, the basic and dilutive losses per common share are the same for the three and six months March 31, 2011. The following is a reconciliation of the numerators and denominators of the basic and diluted EPS computations for continuing and discontinued operations:

	For the three months ended March 31, 2011 (Restated)			For the three months ended March 31, 2010		
	Loss (numerator)	(Unaudited) Weighted Average Shares (denominator)	Per share amount	Loss (numerator)	(Unaudited) Weighted Average Shares (denominator)	Per share amount
Basic and Diluted EPS						
Loss from continuing operations	\$ (1,082,577)	6,990,662	\$ (0.15)	\$ (260,044)	5,992,919	\$ (0.04)
Loss from discontinued operations	\$ (269,134)	6,990,662	\$ (0.04)	\$ (28,427)	5,992,919	\$ -