

AMERICAN TECHNOLOGY CORP /DE/  
Form 10-Q  
April 30, 2009  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**

**FORM 10-Q**

(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, 2009

or

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_.

Commission File Number: 000-24248

**AMERICAN TECHNOLOGY CORPORATION**

(Exact name of registrant as specified in its charter)

Delaware

87-0361799

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(State or other jurisdiction of  
incorporation or organization)

(I.R.S. Employer  
Identification Number)

15378 Avenue of Science, Ste 100, San Diego,

California  
(Address of principal executive offices)

(858) 676-1112

92128  
(Zip Code)

(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 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 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.

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company   
(Do not check if a smaller reporting company)

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 shell company (as defined in Rule 12b-2 of the Exchange Act).  Yes  No

The number of shares of Common Stock, \$0.00001 par value, outstanding on April 23, 2009 was 30,535,207.

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|   | <b>March 31,<br/>2009<br/>(Unaudited)</b> | <b>September 30,<br/>2008</b> |
|---|---|-------------------------------|
| <b>ASSETS</b>   |   |                               |
| <b>Current assets:</b>  |   |                               |
| Cash and cash equivalents   | \$ 2,759,903                              | \$ 2,694,869                  |
| Accounts receivable, less allowance of \$244,214 and \$247,625 for doubtful accounts                                  | 3,444,661                                 | 2,210,526                     |
| Inventories, net  | 2,929,353                                 | 2,890,219                     |
| Prepaid expenses and other  | 264,819                                   | 251,390                       |
| <b>Total current assets</b>   | <b>9,398,736</b>                          | <b>8,047,004</b>              |
| <b>Property and equipment, net</b>  | <b>313,055</b>                            | <b>292,094</b>                |
| <b>Patents, net</b>   | <b>948,911</b>                            | <b>1,058,186</b>              |
| <b>Deposits</b>   | <b>58,265</b>                             | <b>58,265</b>                 |
| <b>Total assets</b>   | <b>\$ 10,718,967</b>                      | <b>\$ 9,455,549</b>           |
| <b>LIABILITIES AND STOCKHOLDERS EQUITY</b>  |   |                               |
| <b>Current liabilities:</b>   |   |                               |
| Accounts payable  | \$ 1,253,341                              | \$ 963,915                    |
| Accrued liabilities   | 871,445                                   | 977,803                       |
| <b>Total current liabilities</b>  | <b>2,124,786</b>                          | <b>1,941,718</b>              |
| <b>Commitments and contingencies (Note 12)</b>  |   |                               |
| <b>Stockholders equity</b>  |   |                               |
| Preferred stock, \$0.00001 par value; 5,000,000 shares authorized: none issued and outstanding                        |   |                               |
| Common stock, \$0.00001 par value; 50,000,000 shares authorized; 30,535,207 shares issued and outstanding each period | 305                                       | 305                           |
| Additional paid-in capital  | 82,457,505                                | 81,374,937                    |
| Accumulated deficit   | (73,863,629)                              | (73,861,411)                  |
| <b>Total stockholders equity</b>  | <b>8,594,181</b>                          | <b>7,513,831</b>              |
| <b>Total liabilities and stockholders equity</b>  | <b>\$ 10,718,967</b>                      | <b>\$ 9,455,549</b>           |

See accompanying notes to interim consolidated financial statements

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## CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

|   | For the three months ended<br>March 31, |                | For the six months ended<br>March 31, |                |
|---|---|----------------|---------------------------------------|----------------|
|   | 2009                                    | 2008           | 2009                                  | 2008           |
| <b>Revenues:</b>  |   |                |                                       |                |
| Product sales   | \$ 5,801,400                            | \$ 1,959,310   | \$ 8,232,243                          | \$ 4,382,997   |
| Contract, license and other                                   | 71,082                                  | 89,062         | 133,482                               | 201,019        |
| Total revenues  | 5,872,482                               | 2,048,372      | 8,365,725                             | 4,584,016      |
| Cost of revenues  | 2,755,625                               | 1,317,319      | 4,106,597                             | 2,699,034      |
| <b>Gross profit</b>   | 3,116,857                               | 731,053        | 4,259,128                             | 1,884,982      |
| <b>Operating expenses:</b>                                    |   |                |                                       |                |
| Selling, general and administrative                           | 1,797,917                               | 1,753,881      | 3,384,877                             | 3,783,234      |
| Research and development                                      | 448,650                                 | 1,166,849      | 901,108                               | 1,977,027      |
| Total operating expenses                                      | 2,246,567                               | 2,920,730      | 4,285,985                             | 5,760,261      |
| Income (loss) from operations                                 | 870,290                                 | (2,189,677)    | (26,857)                              | (3,875,279)    |
| <b>Other income (expense):</b>                                |   |                |                                       |                |
| Interest income   | 8,521                                   | 56,302         | 24,639                                | 126,732        |
| Finance expense   |   |                |                                       | (108,821)      |
| Total other income  | 8,521                                   | 56,302         | 24,639                                | 17,911         |
| <b>Net income (loss)</b>                                      | \$ 878,811                              | \$ (2,133,375) | \$ (2,218)                            | \$ (3,857,368) |
| <b>Net income (loss) per common share - basic and diluted</b> | \$ 0.03                                 | \$ (0.07)      | \$ 0.00                               | \$ (0.13)      |
| <b>Weighted average common shares outstanding</b>             |   |                |                                       |                |
| <b>Basic</b>  | 30,535,207                              | 30,535,207     | 30,535,207                            | 30,535,207     |
| <b>Diluted</b>  | 30,611,648                              | 30,535,207     | 30,535,207                            | 30,535,207     |

See accompanying notes to interim consolidated financial statements

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## CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

|   | <b>For the six months ended<br/>March 31,</b> |                |
|---|---|----------------|
|   | <b>2009</b>                                   | <b>2008</b>    |
| <b>Increase (Decrease) in cash and cash equivalents:</b>                    |   |                |
| <b>Operating activities:</b>  |   |                |
| Net loss  | \$ (2,218)                                    | \$ (3,857,368) |
| Adjustments to reconcile net loss to net cash used in operating activities: |   |                |
| Depreciation and amortization   | 151,748                                       | 198,005        |
| Provision for doubtful accounts   | (3,410)                                       | (5,632)        |
| Warranty provision  | 44,041  | (25,705)       |
| Inventory obsolescence  | 27,026  | (27,273)       |
| Share-based compensation  | 1,082,568                                     | 1,144,404      |
| Loss on impairment of patents   | 75,744  | 205,521        |
| Changes in assets and liabilities:  |   |                |
| Accounts receivable   | (1,230,725)                                   | (733,541)      |
| Inventories   | (66,160)                                      | 84,834         |
| Prepaid expenses and other  | (13,429)                                      | (57,137)       |
| Accounts payable  | 289,426                                       | 676,786        |
| Warranty settlements  | (11,513)                                      | (21,498)       |
| Accrued liabilities   | (138,886)                                     | 668,656        |
| Net cash provided by (used in) operating activities                         | 204,212                                       | (1,749,948)    |
| <b>Investing activities:</b>  |   |                |
| Purchase of equipment   | (118,048)                                     | (89,692)       |
| Patent costs paid   | (21,130)                                      | (117,766)      |
| Net cash used in investing activities                                       | (139,178)                                     | (207,458)      |
| Net increase (decrease) in cash and cash equivalents                        | 65,034  | (1,957,406)    |
| Cash and cash equivalents, beginning of period                              | 2,694,869                                     | 6,414,537      |
| Cash and cash equivalents, end of period                                    | \$ 2,759,903                                  | \$ 4,457,131   |

See accompanying notes to interim consolidated financial statements

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**American Technology Corporation**

**Notes to Interim Consolidated Financial Statements (unaudited)**

**1. OPERATIONS**

American Technology Corporation, a Delaware corporation (the "Company"), is engaged in the design, development and commercialization of directed sound technologies and products. The principal markets for the Company's proprietary sound reproduction technologies and products are in North America, Europe and Asia. The Company operates its business in one operating segment.

The Company has a wholly owned subsidiary, American Technology Holdings, Inc., through which the Company intends to conduct international marketing, sales and distribution activities. The consolidated financial statements include the accounts of this subsidiary after elimination of intercompany transactions and accounts.

**2. STATEMENT OF PRESENTATION AND MANAGEMENT'S PLAN**

The accompanying unaudited interim consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and the instructions to Form 10-Q and Article 8 of Regulation S-X. In the opinion of management, the interim financial statements reflect all adjustments necessary in order to make the financial statements not misleading. The consolidated balance sheet as of September 30, 2008 was derived from the Company's most recent audited financial statements. Operating results for the three and six month period are not necessarily indicative of the results that may be expected for the year. The interim financial statements and notes thereto should be read in conjunction with the Company's audited financial statements and notes thereto for the year ended September 30, 2008 included in the Company's Annual Report on Form 10-K, as filed with the Securities and Exchange Commission ("SEC") on December 4, 2008.

The Company recorded net income of \$878,811 in the three months ended March 31, 2009 and in the six months ended March 31, 2009, recorded a net increase in cash and cash equivalents of \$65,034. For the six months ended March 31, 2009 and 2008, the Company incurred net losses of \$2,218 and \$3,857,368, respectively. Management believes the Company has adequate financial resources to execute its fiscal 2009 operating plan and to sustain operations for the next twelve months. Management's operating plan includes (a) growing revenues by focusing on the U.S. military and direct sales to larger commercial and defense related companies, (b) improving product margins by reducing unit product costs and monitoring manufacturing overhead, and (c) controlling research and development and selling, general and administrative costs. Nevertheless, the Company's operating results will depend on future product sales levels and other factors, some of which are beyond the Company's control. There can be no assurance the Company can continue to achieve positive cash flow or profitability. The Company operates in a rapidly evolving and often unpredictable business environment that may change the timing or amount of expected future cash receipts and expenditures. If required, management has some flexibility to take remedial actions to adjust the level of research and development and selling, general and administrative expenses based on the availability of resources. However, there can be no assurance that the Company may not be required to raise additional funds through the sale of equity or debt securities or from credit facilities. Additional capital, if needed, may not be available on satisfactory terms, or at all.

**3. RECENT ACCOUNTING PRONOUNCEMENTS**

In September 2006, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 157, Fair Value Measurements ("SFAS No. 157"). This standard defines fair value, establishes a framework for measuring fair value in accounting principles generally accepted in the United States of America, and expands disclosure about fair value measurements. According to the original pronouncement, SFAS No. 157 was effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. In February 2008, the FASB issued FSP FAS 157-2 which defers the effective date of SFAS No. 157 for all non-financial assets and liabilities, except those items recognized or disclosed at fair value on an annual or more frequent recurring basis, until years beginning after November 15, 2008. The Company's adoption of SFAS No. 157 for its financial assets and liabilities on October 1, 2008 did not have a material impact on the Company's consolidated financial statements. The Company is currently reviewing the adoption requirements related to its non-financial assets and liabilities and has not yet determined the impact, if any, this will have on its consolidated financial statements.

In October 2008, the FASB issued FASB Staff Position ("FSP") SFAS 157-3, Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active ("FSP SFAS 157-3"). FSP SFAS 157-3 clarifies the application of SFAS No. 157, Fair Value Measurements, in a market that is not active and provides an example to illustrate key considerations in determining the fair value of a financial asset when the market for that financial asset is not active. FSP SFAS 157-3 is effective upon issuance, including for prior periods for which financial

statements have not been issued.



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Revisions resulting from a change in the valuation technique or its application should be accounted for as a change in accounting estimate following the guidance in SFAS No. 154, *Accounting Changes and Error Corrections* ( SFAS No. 154 ). However, the disclosure provisions in SFAS No. 154 for a change in accounting estimate are not required for revisions resulting from a change in valuation technique or its application. The adoption of this pronouncement by the Company did not have a material effect on its consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115* ( SFAS No. 159 ), which will permit the option of choosing to measure certain eligible items at fair value at specified election dates and report unrealized gains and losses in earnings. SFAS No. 159 became effective for the Company on October 1, 2008. The adoption of SFAS No. 159 did not have a material impact on the Company's consolidated financial statements.

In April 2008, the FASB issued FSP FAS 142-3, *Determination of Useful Life of Intangible Assets* ( FSP FAS 142-3 ). FSP FAS 142-3 amends the factors that should be considered in developing the renewal or extension assumptions used to determine the useful life of a recognized intangible asset under SFAS 142, *Goodwill and Other Intangible Assets*. FSP FAS 142-3 also requires expanded disclosure related to the determination of intangible asset useful lives. FSP FAS 142-3 is effective for fiscal years beginning after December 15, 2008. Earlier adoption is not permitted. The Company does not expect FSP FAS 142-3 to have a material impact on its consolidated financial statements.

In June 2008, the FASB ratified EITF Issue No. 07-5, *Determining whether an Instrument (or Embedded Feature) is Indexed to an Entity's Own Stock* ( EITF 07-5 ). EITF 07-5 is effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years. Early application is not permitted. EITF 07-5 provides a new two-step model to be applied in determining whether a financial instrument or an embedded feature is indexed to an issuer's own stock and thus able to qualify for the SFAS No. 133 paragraph 11(a) scope exception. The Company has not completed an analysis of this pronouncement nor determined the effects of pending adoption, if any, on its consolidated financial statements.

**4. INVENTORIES**

Inventories are stated at the lower of cost, which approximates actual costs on a first in, first out cost basis, or market. Inventories consisted of the following:

|                          | March 31,<br>2009 | September 30,<br>2008 |
|--------------------------|-------------------|-----------------------|
| Finished goods           | \$ 1,074,882      | \$ 998,609            |
| Work in process          | 57,292            | 29,959                |
| Raw materials            | 3,379,356         | 3,416,802             |
|                          | 4,511,530         | 4,445,370             |
| Reserve for obsolescence | (1,582,177)       | (1,555,151)           |
| Total, net               | \$ 2,929,353      | \$ 2,890,219          |

**5. PROPERTY AND EQUIPMENT**

Property and equipment consisted of the following:

|                                | March 31,<br>2009 | September 30,<br>2008 |
|--------------------------------|-------------------|-----------------------|
| Machinery and equipment        | \$ 620,126        | \$ 511,464            |
| Office furniture and equipment | 828,839           | 821,121               |
| Leasehold improvements         | 262,258           | 260,591               |
|                                | 1,711,223         | 1,593,176             |
| Accumulated depreciation       | (1,398,168)       | (1,301,082)           |

|                             |            |            |
|-----------------------------|------------|------------|
| Property and equipment, net | \$ 313,055 | \$ 292,094 |
|-----------------------------|------------|------------|

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Included in office furniture and equipment at March 31, 2009 and September 30, 2008 was \$417,937 and \$411,963, respectively, for purchased software, which is being amortized over three years. The unamortized portion of software at March 31, 2009 and September 30, 2008 was \$13,629 and \$13,755, respectively.

Depreciation expense, excluding amortization of software, was \$90,986 and \$118,717 for the six months ended March 31, 2009 and 2008, respectively. Amortization of purchased software was \$6,101 and \$16,868 for the six months ended March 31, 2009 and 2008, respectively.

**6. PATENTS**

Patents consisted of the following:

|                          | March 31,<br>2009 | September 30,<br>2008 |
|--------------------------|-------------------|-----------------------|
| Cost                     | \$ 1,588,001      | \$ 1,662,787          |
| Accumulated amortization | (639,090)         | (604,601)             |
| <b>Patents, net</b>      | <b>\$ 948,911</b> | <b>\$ 1,058,186</b>   |

Amortization expense for the Company's patents was \$54,661 and \$62,420 for the six months ended March 31, 2009 and 2008, respectively.

Each quarter, the Company reviews the ongoing value of its capitalized patent costs. In the first six months of fiscal 2009, some of these assets were identified as being associated with patents that are no longer consistent with its business strategy. As a result of this review, the Company reduced the value of previously capitalized patents by \$75,744 during the six months ended March 31, 2009, compared to a reduction of \$205,521 from the impairment of patents in the six months ended March 31, 2008.

**7. SHARE-BASED COMPENSATION***Stock Option Plans*

At March 31, 2009, the Company had two equity incentive plans. The 2002 Stock Option Plan ( 2002 Plan ) was terminated with respect to new grants in April 2005 but remains in effect for grants issued prior to that time. The 2005 Equity Incentive Plan ( 2005 Plan ), as amended, authorizes for issuance as stock options, stock appreciation rights, or stock awards an aggregate of 3,250,000 new shares of common stock to employees, directors or consultants, plus the 1,749,564 shares remaining eligible for issuance under the 2002 Plan for a total plan reserve of 4,999,564. The current plan reserve at March 31, 2009, net of exercises, allows for the issuance of up to 4,644,663 shares. At March 31, 2009, there were options outstanding covering 98,000 and 3,958,262 shares of common stock under the 2002 Plan and 2005 Plan, respectively.

At March 31, 2009, there were also options outstanding covering 32,000 shares of common stock from grants outside the stock option plans. See Note 8 for summary stock option activity during the six months ended March 31, 2009.

**Table of Contents***Share-Based Payments*

The Company accounts for share-based payments under the provisions of SFAS No. 123(R) Share-based payments ( SFAS 123(R) ). Options or stock awards issued to non-employees who are not directors of the Company are recorded at their estimated fair value at the measurement date in accordance with SFAS No. 123(R) and EITF Issue No. 96-18, Accounting for Equity Instruments That Are Issued to Other Than Employees for Acquiring or in Conjunction with Selling Goods or Services, and are periodically revalued as the options vest and are recognized as expense over the related service period. The Company recorded \$1,082,568 and \$1,144,404 of share-based compensation expense for the six months ended March 31, 2009 and 2008, respectively. The amounts of share-based compensation expense are classified in the consolidated statements of operations as follows:

|                                     | Three Months Ended<br>March 31, |            | Six Months Ended<br>March 31, |              |
|-------------------------------------|---------------------------------|------------|-------------------------------|--------------|
|                                     | 2009                            | 2008       | 2009                          | 2008         |
| Cost of revenue                     | \$ 20,067                       | \$ 22,068  | \$ 38,628                     | \$ 39,743    |
| Selling, general and administrative | 461,325                         | 511,396    | 964,952                       | 984,355      |
| Research and development            | 32,920                          | 63,585     | 78,988                        | 120,306      |
| Total                               | \$ 514,312                      | \$ 597,049 | \$ 1,082,568                  | \$ 1,144,404 |

The weighted-average estimated fair value of employee stock options granted during the six months ended March 31, 2009 and 2008 was \$0.24 and \$0.96, per share, respectively, using the Black-Scholes option pricing model with the following weighted-average assumptions (annualized percentages):

|                         | Six months ended March 31, |               |
|-------------------------|----------------------------|---------------|
|                         | 2009                       | 2008          |
| Volatility              | 71.0%                      | 71.0%         |
| Risk-free interest rate | 1.30% - 1.52%              | 2.79% - 3.49% |
| Forfeiture rate         | 20.0%                      | 20.0%         |
| Dividend yield          | 0.0%                       | 0.0%          |
| Expected life in years  | 3.4 - 4.9                  | 3.4 - 4.9     |

The dividend yield of zero is based on the fact that the Company has never paid cash dividends and has no present intention to pay cash dividends. Expected volatility is based on the historical volatility of the Company's common stock over the period commensurate with the expected life of the options. The risk-free interest rate is based on rates published by the Federal Reserve Board. The expected life is based on observed and expected time to post-vesting exercise. The expected forfeiture rate is based on past experience and employee retention data. Forfeitures are estimated at the time of the grant and revised in subsequent periods if actual forfeitures differ from those estimates or if the Company updates its estimated forfeiture rate. Such amounts will be recorded as a cumulative adjustment in the period in which the estimate is changed.

Since the Company has a net operating loss carryforward as of March 31, 2009, no excess tax benefit for the tax deductions related to share-based awards was recognized for the six months ended March 31, 2009 and 2008. Additionally, as there were no options exercised in the six months ended March 31, 2009 or 2008, there were no incremental tax benefits recognized. Such recognition would have resulted in a reclassification to reduce net cash provided by operating activities with an offsetting increase in net cash provided by financing activities.

As of March 31, 2009, there was \$900,000 of total unrecognized compensation cost related to non-vested share-based employee compensation arrangements. The cost is expected to be recognized over a weighted-average period of 1.4 years.

**Table of Contents****8. STOCKHOLDERS EQUITY***Summary*

The following table summarizes changes in stockholders' equity components during the six months ended March 31, 2009:

|                                     | Common Stock |        | Additional         | Accumulated     | Total                   |
|-------------------------------------|--------------|--------|--------------------|-----------------|-------------------------|
|                                     | Shares       | Amount | Paid-in<br>Capital | Deficit         | Stockholders'<br>Equity |
| <b>Balances, September 30, 2008</b> | 30,535,207   | \$ 305 | \$ 81,374,937      | \$ (73,861,411) | \$ 7,513,831            |
| Share-based compensation expense    |              |        | 1,082,568          |                 | 1,082,568               |
| Net loss for the period             |              |        |                    | (2,218)         | (2,218)                 |
| <b>Balances, March 31, 2009</b>     | 30,535,207   | \$ 305 | \$ 82,457,505      | \$ (73,863,629) | \$ 8,594,181            |

*Common Stock Activity*

There was no common stock activity during the six months ended March 31, 2009.

*Stock Option Activity*

The following table summarizes information about stock option activity during the six months ended March 31, 2009:

|  | Number<br>of<br>Shares | Weighted Average<br>Exercise Price |
|--|------------------------|------------------------------------|
| <b>Fiscal 2009:</b>  |                        |                                    |
| Outstanding October 1, 2008                                    | 3,226,200              | \$ 3.72                            |
| Granted  | 955,000                | \$ 0.48                            |
| Canceled/expired   | (92,938)               | \$ 3.37                            |
| <b>Outstanding March 31, 2009</b>                              | <b>4,088,262</b>       | <b>\$ 2.97</b>                     |
| Exercisable at March 31, 2009                                  | 3,014,017              | \$ 3.43                            |
| Weighted average fair value of options granted during the year |                        | \$ 0.24                            |

Options outstanding are exercisable at prices ranging from \$0.46 to \$9.48 and expire over the period from 2009 to 2013 with an average life of 3.32 years. The aggregate intrinsic value of options outstanding and exercisable at March 31, 2009 was \$245,923 and \$100,667, respectively.

*Stock Purchase Warrants*

There was no warrant activity during the six months ended March 31, 2009. The number of shares purchasable under outstanding warrants at March 31, 2009 was 2,936,693 at a weighted average purchase price of \$3.78.

At March 31, 2009, the following stock purchase warrants were outstanding arising from offerings and other transactions:

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| <b>Number</b> | <b>Exercise Price</b> | <b>Expiration Date</b> |
|---------------|-----------------------|------------------------|
| 838,489       | \$ 5.44*              | July 18, 2009          |
| 75,000        | \$ 8.60               | December 31, 2009      |
| 75,000        | \$ 9.28               | December 31, 2009      |
| 1,948,204     | \$ 2.67*              | August 7, 2010         |
| 2,936,693     |                       |                        |

\* These warrants contain antidilution rights if the Company sells securities for less than the exercise price.

**Table of Contents****9. ACCRUED LIABILITIES**

Accrued liabilities consisted of the following:

|                     | March 31,<br>2009 | September 30,<br>2008 |
|---------------------|-------------------|-----------------------|
| Payroll and related | \$ 257,900        | \$ 421,686            |
| Deferred revenue    | 275,509           | 275,509               |
| Warranty reserve    | 267,702           | 235,174               |
| Customer deposits   | 40,712            | 8,975                 |
| Other               | 29,622            | 36,459                |
| <b>Total</b>        | <b>\$ 871,445</b> | <b>\$ 977,803</b>     |

Changes in the warranty reserve during the three and six months ended March 31, 2009 and 2008 were as follows:

|                       | Three Month Ended<br>March 31, |                   | Six Months Ended<br>March 31, |                   |
|-----------------------|--------------------------------|-------------------|-------------------------------|-------------------|
|                       | 2009                           | 2008              | 2009                          | 2008              |
| Beginning balance     | \$ 239,186                     | \$ 140,990        | \$ 235,174                    | \$ 182,247        |
| Warranty provision    | 35,861                         | (1,918)           | 44,041                        | (25,705)          |
| Warranty settlements  | (7,345)                        | (4,028)           | (11,513)                      | (21,498)          |
| <b>Ending balance</b> | <b>\$ 267,702</b>              | <b>\$ 135,044</b> | <b>\$ 267,702</b>             | <b>\$ 135,044</b> |

**10. INCOME (LOSS) PER SHARE**

Basic earnings (loss) per share is computed by dividing net income (loss) by the weighted average number of common shares outstanding for the period. Diluted earnings (loss) per share is computed by dividing net income (loss) by the weighted-average number of shares of common stock outstanding during the period increased to include the number of dilutive potential common shares outstanding during the period. The dilutive effect of outstanding stock options and warrants is reflected in diluted earnings per share by application of the treasury stock method, which assumes that the proceeds from the exercise of the outstanding options and warrants are used to repurchase common stock at market value. Under the treasury stock method, an increase in the fair market value of the Company's common stock can result in a greater dilutive effect from potentially dilutive securities. The Company's losses for certain periods presented cause the inclusion of potential common stock instruments outstanding to be antidilutive.

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

|  | Three Months Ended<br>March 31, |                | Six Months Ended<br>March 31, |                |
|--|---------------------------------|----------------|-------------------------------|----------------|
|  | 2009                            | 2008           | 2009                          | 2008           |
| <b>Basic</b>                                       |                                 |                |                               |                |
| Net income (loss)                                  | \$ 878,811                      | \$ (2,133,375) | \$ (2,218)                    | \$ (3,857,368) |
| Weighted average common shares outstanding (basic) | 30,535,207                      | 30,535,207     | 30,535,207                    | 30,535,207     |
| Basic income (loss) per common share               | \$ 0.03                         | \$ (0.07)      | \$ (0.00)                     | \$ (0.13)      |
| <b>Diluted</b>                                     |                                 |                |                               |                |

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|   |            |                |            |                |
|---|------------|----------------|------------|----------------|
| Net income (loss)   | \$ 878,811 | \$ (2,133,375) | \$ (2,218) | \$ (3,857,368) |
| Weighted average common shares outstanding  | 30,535,207 | 30,535,207     | 30,535,207 | 30,535,207     |
| Assumed exercise of options   | 76,441     |                |            |                |
| Common and potential common shares  | 30,611,648 | 30,535,207     | 30,535,207 | 30,535,207     |
| Diluted income (loss) per common share  | \$ 0.03    | \$ (0.07)      | \$ (0.00)  | \$ (0.13)      |
| Potentially dilutive stock options and warrants outstanding at period end excluded from diluted computation as they were antidilutive | 6,074,329  | 6,408,954      | 7,024,955  | 6,408,954      |



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### **11. MAJOR CUSTOMERS**

For the three and six months ended March 31, 2009, revenues from one customer accounted for 42% and 33% of revenues, respectively, with no other single customer accounting for more than 10% of revenues. At March 31, 2009, accounts receivable from one customer accounted for 56% of total accounts receivable, with no other single customer accounting for more than 10% of the accounts receivable balance.

For the three months ended March 31, 2008, revenues from two customers accounted for 25% and 18% of revenues, respectively; and for the six months ended March 31, 2008, revenues from three customers accounted for 15%, 11% and 11%, respectively, with no other single customer accounting for more than 10% of revenues. At March 31, 2008, accounts receivable from three customers accounted for 27%, 15% and 12% of total accounts receivable with no other single customer accounting for more than 10% of the accounts receivable balance.

### **12. COMMITMENTS AND CONTINGENCIES**

#### *Bank and Other Cash Equivalent Deposits in Excess of FDIC Insurance Limits*

The Company currently maintains its cash and cash equivalent accounts with a major financial institution. Effective October 14, 2008, Federal Deposit Insurance Corporation deposit insurance was changed to provide full deposit insurance coverage for non-interest bearing deposit transaction accounts through December 31, 2009. Also in October 2008, the financial institution enrolled in the U.S. Treasury Department's Temporary Guarantee Program for money market funds. Under this program, the U.S. Treasury guarantees the \$1.00 per share value of fund shares outstanding as of September 19, 2008, subject to certain terms and limitations. As a result, since all of the Company's cash equivalents at March 31, 2009 consist of money market funds with this financial institution, these funds are guaranteed at 100% up to the balance held as of September 19, 2008. Based on these changes, as of March 31, 2009, the Company did not have any cash and cash equivalents that are either in excess of current FDIC limits or that are not guaranteed by the U.S. Treasury Department.

#### *Litigation*

The Company may at times be involved in litigation in the ordinary course of business. The Company will, from time to time, when appropriate in management's estimation, record adequate reserves in the Company's financial statements for pending litigation. Currently, there are no pending material legal proceedings to which the Company is a party or to which any of its property is subject.

### **Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

The following discussion should be read in conjunction with the accompanying unaudited interim financial statements and the related notes included under Item 1 of this Quarterly Report on Form 10-Q, together with Management's Discussion and Analysis of Financial Condition and Results of Operations included in our Annual Report on Form 10-K for the year ended September 30, 2008.

The following discussion provides an overview of our results of operations for the three and six months ended March 31, 2009 and 2008. Significant period-to-period variances in the consolidated statements of operations are discussed under the caption Results of Operations. Our financial condition and cash flows are discussed under the caption Liquidity and Capital Resources.

### **Forward Looking Statements**

*This report contains certain statements of a forward-looking nature relating to future events or future performance. Words such as expects, anticipates, intends, plans, believes, seeks, estimates and similar expressions or variations of such words are intended to identify forward-looking statements, but are not the only means of identifying forward-looking statements. Prospective investors are cautioned that such statements are only predictions and that actual events or results may differ materially. In evaluating such statements, prospective investors should specifically consider various factors identified in this report and any matters set forth under Part I, Item 1A (Risk Factors) of our Annual Report on Form 10-K, which could cause actual results to differ materially from those indicated by such forward-looking statements.*

### **Overview**

We are a pioneer of highly intelligible, high clarity, directed sound technologies and products. We aggressively seek to create markets for our products, and we are increasing our focus on and investment in worldwide sales and marketing activities while we continue to innovate.

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During 2008, we completed the development of a new generation of LRAD® products called the LRAD-X®. Our new LRAD-X products use directionality and focused acoustic output to clearly transmit critical information, instructions and warnings 500 meters and beyond. The LRAD-X product line can be manually operated or integrated into a remotely controlled security network's command and control center. Through the use of powerful voice commands and deterrent tones, large safety zones can be created while determining the

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intent and influencing the behavior of an intruder. Our LRAD- X products are the industry's loudest, most intelligible line of directed acoustic hailing and warning devices (AHDs), and feature rugged, weatherproof construction and enhanced voice, tone and frequency response. Our new product line includes the following:

**LRAD 1000X** selected by the U.S. Navy as its AHD for Block 0 of the Shipboard Protection System can be manually operated to provide long distance hailing and warning with highly intelligible communication.

**LRAD 500X** selected by the U.S. Navy and U.S. Army as their AHD for small vessels and vehicles is lightweight and can be easily transported to provide security personnel long-range communications and a highly effective hailing and warning capability where needed.

**LRAD 100X** is portable and designed for use in a variety of mass notification and commercial security applications. It is ideally suited for short-range perimeter security and it adds highly intelligible sound/communication resources into traditional camera-based security networks in an integrated package.

**LRAD RX** is our prescription for remotely controlled security. It enables system operators to detect and communicate with an intruder over long distances. LRAD-RX features an LRAD 1000X emitter head and an integrated IP-addressable full pan and tilt drive system for precise aiming and tracking. LRAD-RX reduces manpower and false alarms while providing an intelligent, cost-effective security solution. The LRAD-RX can be operated remotely from anywhere across a TCP/IP network enabling system operators to respond to security threats from a safe remote environment. The LRAD-RX is aimed and controlled by our proprietary pan and tilt drive system. We designed and engineered this pan and tilt drive system during fiscal 2008 to meet the demanding specifications of customers that deploy these devices on large vessels, offshore oil and other platforms. The LRAD-RX can be integrated with a number of other sensors (radar, camera, etc.) creating a fully integrated unmanned perimeter security solution.

These products have been well received by our military customers and interest has been strong for other applications such as oil rig protection, maritime and homeland security, port security, bird and wildlife deterrents and by law enforcement. We believe these products provide an increased opportunity for us in both the government and commercial markets that we are developing, and will allow us to continue as the leader in this market. We believe that our products are offered at price and performance points to attract serious market interest. Accelerating our product sales and revenue growth will require organizational discipline, improved customer focus, and a new, sustained marketing push of our Company and products. We are focused on these areas of our business while also containing costs.

As has been widely reported, financial markets in the United States, Europe and Asia have been experiencing extreme disruption in recent months, including, among other things, extreme volatility in security prices, severely diminished liquidity and credit availability, rating downgrades of certain investments and declining valuations of others. Governments have taken unprecedented actions intended to address extreme market conditions that include severely restricted credit and declines in real estate values. While currently these conditions have not impaired our ability to operate our business, there can be no assurance that there will not be a further deterioration in financial markets and confidence in major economies, which can then lead to challenges in the operation of our business. These economic developments affect businesses such as ours in a number of ways. The current tightening of credit in financial markets adversely affects the ability of commercial customers to finance purchases and operations and could result in a decrease in orders and spending for our products as well as create supplier disruptions. Economic developments could also reduce future government spending on our products. We are unable to predict the likely duration and severity of the current disruption in financial markets and adverse economic conditions and the effects they will have on our business and financial condition.

### **Overall Performance for the Second Quarter of Fiscal 2009**

For our second fiscal quarter ended March 31, 2009:

Our revenues for the three months ended March 31, 2009 increased 187% to \$5,872,482 from \$2,048,372 for the three months ended March 31, 2008. The revenue growth was in our LRAD product line, partially offset by reductions in our HSS and SoundSaber

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product lines. In addition to strong sales to the U.S. Navy and Army, we have continued to diversify our revenues to foreign military groups, shipping companies, fisheries, police and other commercial applications.

We recorded a gross profit of \$3,116,857 for the three months ended March 31, 2009 (53% of revenues), which was \$2,385,804 higher than \$731,053 for the quarter ended March 31, 2008 (36% of revenues), driven by higher revenues, increased product margins and better fixed overhead absorption.

Operating expenses of \$2,246,567 for the three months ended March 31, 2009 decreased by \$674,163 or 23% from the three months ended March 31, 2008. The prior year included an additional \$343,187 related to the development of our LRAD-X product line launched last year. In addition, we had savings of \$329,530 from reduced staffing levels, \$115,249 from reduced impairment of patents, \$92,267 from lower professional fees due to a change in audit firms and other savings, offset by an increase in third party sales commissions of \$445,897.

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We generated net income for the first time in the Company's history during the quarter ended March 31, 2009. Our net income during this period of \$878,811, or \$0.03 per share was an increase of \$3,012,186 compared to the net loss of \$2,133,375, or \$0.07 per share, for the quarter ended March 31, 2008, due to the increased revenues and gross profit and reduction in operating expenses described above.

For the three month period ended March 31, 2009, we increased our cash and cash equivalents by \$318,596, primarily due to our net income for the period and close management of working capital. Net income (losses) and changes in working capital components cause significant variances in operating cash on a quarter over quarter basis.

Our various technologies are high risk in nature. However, we believe we have a solid technology and product foundation for business growth over the next several years. We have additional new technologies and products in various stages of development. We believe we have strong market opportunities, particularly given the continuing global threats to both governments and commerce, where our LRAD products have proven to be effective at determining intent and hailing and notification for force protection.

### **Critical Accounting Policies**

We have identified a number of accounting policies as critical to our business operations and the understanding of our results of operations. These are described in our consolidated financial statements located in Item 1 of Part I, Financial Statements, and Management's Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report of Form 10-K for the year ended September 30, 2008. The impact and any associated risks related to these policies on our business operations is discussed throughout Management's Discussion and Analysis of Financial Condition and Results of Operations when such policies affect our reported and expected financial results.

The methods, estimates and judgments we use in applying our accounting policies, in conformity with generally accepted accounting principles in the United States, have a significant impact on the results we report in our financial statements. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. The estimates affect the carrying values of assets and liabilities. Actual results may differ from these estimates under different assumptions or conditions.

### **Results of Operations for the Three Months Ended March 31, 2009 and 2008**

#### ***Revenues***

Revenues for the three months ended March 31, 2009 were \$5,872,482, representing a 187% increase from \$2,048,372 in revenues for the three months ended March 31, 2008. Revenues for the three months ended March 31, 2009 included \$5,801,400 of product sales and \$71,082 of contract, license and other revenues. Revenues for the three months ended March 31, 2008 included \$1,959,310 of product sales and \$89,062 of contract, license and other revenues. The revenue growth was in our LRAD product line, partially offset by reductions in our HSS and SoundSaber product lines. In addition to strong sales to the U.S. Navy and Army, we have continued to diversify our revenues to foreign military groups, shipping companies, fisheries, police and other commercial applications. Our revenues are highly dependent on the timing of large orders from a small number of customers. We expect continued uneven quarterly revenues in future periods due to the lack of established markets for our proprietary products.

For the three months ended March 31, 2008, we recognized \$54,167 in contract revenue representing ratable earned revenue under a three year license agreement. We did not record any similar contract revenue in the three months ended March 31, 2009 as the contract expired in September 2008. At March 31, 2009, there was no revenue unearned under this agreement. At March 31, 2009, we had aggregate deferred license revenue of \$275,509 representing amounts collected from another license agreement in advance of recognized earnings. This revenue component is subject to significant variability based on the timing, amount and recognition of new arrangements, if any.

#### ***Gross Profit***

Gross profit for the three months ended March 31, 2009 was \$3,116,857, or 53% of revenues, compared to \$731,053, or 36% of revenues, for the three months ended March 31, 2008. The increase in gross profit was driven by higher revenues, increased product margins due to reduced product cost and favorable mix, and broader absorption of our fixed overhead expenses as a result of the higher revenues.

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Our products have varying gross margins, so product sales mix will materially affect gross profits. In addition, we continue to make product updates and changes, including raw material and component changes that may impact product costs. With such product updates and changes we have limited warranty cost experience and estimated future warranty costs can impact our gross margins. We do not believe that historical gross profit margins should be relied upon as an indicator of future gross profit margins.

### ***Selling, General and Administrative Expenses***

Selling, general and administrative expenses for the three months ended March 31, 2009 increased \$44,036 to \$1,797,917, or 31% of revenues, compared to \$1,753,881, or 86% of revenues, for the three months ended March 31, 2008. The increase in selling general and administrative expenses was primarily attributed to \$445,897 increase in outside sales commissions, partially offset by \$102,501 lower salaries and consulting expense, \$92,267 lower professional fees resulting primarily from a change in audit firms, \$72,311 reduced marketing expenses, and other cost savings.

We incurred non-cash share-based compensation expenses related to SFAS No. 123(R) allocated to selling, general and administrative expenses in the three months ended March 31, 2009 and 2008 of \$461,325 and \$511,396, respectively.

We may expend additional resources on marketing and selling our products in future periods as we identify ways to optimize our potential opportunity. This may result in increased selling, general and administrative expenses in the future. Commission expense will vary based on the sales channel and revenue levels.

### ***Research and Development Expenses***

Research and development expenses decreased \$718,199 to \$448,650, or 8% of revenues, for the three months ended March 31, 2009, compared to \$1,166,849, or 57% of revenues, for the three months ended March 31, 2008. This decrease in research and development expense was primarily due to \$343,187 higher consulting, prototypes and testing costs in the prior year for the development of our new LRAD-X product line, \$227,029 in lower salaries and benefits from reduced headcount, and \$115,250 from the reduction in expenses incurred for impairment of patents.

Included in research and development expenses for the three months ended March 31, 2009 and 2008 was \$32,920 and \$63,585 of SFAS No. 123(R) non-cash share-based compensation costs, respectively.

Each quarter, we review the ongoing value of our capitalized patent costs and in the second quarter identified some of these assets as being associated with patents that are no longer consistent with our business strategy. As a result of this review, we reduced the value of our previously capitalized patents by \$39,291 during the quarter ended March 31, 2009, compared to an impairment of \$154,541 in the three months ended March 31, 2008.

Research and development costs vary period to period due to the timing of projects, the availability of funds for research and development and the timing and extent of use of outside consulting, design and development firms. We completed the development of the LRAD-X product line in the third fiscal quarter of 2008 with enhanced performance and louder, more intelligible communications. Based on current plans and reduced engineering staffing, we expect research and development costs to continue in the current fiscal year at a lower level than last year.

### ***Income (Loss) from Operations***

Income from operations was \$870,290 for the three months ended March 31, 2009, compared to loss from operations of \$2,189,677 for the three months ended March 31, 2008. The income from operations is primarily attributable to the increase in revenues, improved gross profit margins and reduced research and development expense.

### ***Other Income***

During the three months ended March 31, 2009, we earned \$8,521 of interest income on our cash and cash equivalents balances compared to \$56,302 during the three months ended March 31, 2008 due to lower cash balances and lower interest rates.

### ***Net Income (Loss)***

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The net income for the three months ended March 31, 2009 was \$878,811, or \$0.03 per share, an increase of \$3,012,186 from a net loss of \$2,133,375, or \$0.07 per share, for the three months ended March 31, 2008. The net income was primarily the result of increased revenues, improved gross profit margins and reduced research and development expense. We had no income tax expense for either of the periods presented.

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### **Results of Operations for the Six Months Ended March 31, 2009 and 2008**

#### ***Revenues***

Revenues for the six months ended March 31, 2009 were \$8,365,725, representing an 82% increase from \$4,584,016 in revenues for the six months ended March 31, 2008. Revenues for the six months ended March 31, 2009 included \$8,232,243 of product sales and \$133,482 of contract, license and other revenues. Revenues for the six months ended March 31, 2008 included \$4,382,997 of product sales and \$201,019 of contract, license and other revenues. Sales increased in our LRAD product line and decreased in our HSS and SoundSaber product lines. We expect continued uneven quarterly revenues in future periods as we continue to develop the markets for our proprietary products.

For the six months ended March 31, 2008, we recognized \$108,334 in contract revenue representing ratable earned revenue under a six year license agreement. We did not record any similar contract revenue in the six months ended March 31, 2009 as the contract expired in September 2008. At March 31, 2009, there was no revenue unearned under this agreement. At March 31, 2009, we had aggregate deferred license revenue of \$275,509 representing amounts collected from another license agreement in advance of recognized earnings. This revenue component is subject to significant variability based on the timing, amount and recognition of new arrangements, if any.

#### ***Gross Profit***

Gross profit for the six months ended March 31, 2009 was \$4,259,128, or 51% of revenues, compared to \$1,884,982, or 41% of revenues, for the six months ended March 31, 2008. The increase in gross profit was due to higher revenues, increased product margins due to reduced product cost and favorable mix and greater absorption of our fixed overhead expenses as a result of the higher revenues.

Our products have varying gross margins, so product sales mix will materially affect gross profits. In addition, we continue to make product updates and changes, including raw material and component changes that may impact product costs. With such product updates and changes we have limited warranty cost experience and estimated future warranty costs can impact our gross margins. We do not believe that historical gross profit margins should be relied upon as an indicator of future gross profit margins.

#### ***Selling, General and Administrative Expenses***

Selling, general and administrative expenses for the six months ended March 31, 2009 decreased \$398,357 to \$3,384,877, or 40% of revenues, compared to \$3,783,234, or 83% of revenues, for the six months ended March 31, 2008. The decrease in selling general and administrative expenses was primarily attributed to \$361,554 in lower professional fees resulting from a change in audit firms, \$228,122 from reduced staffing levels, \$120,053 from lower marketing expenses and other expense reductions, partially offset by an increase of \$490,690 in outside sales commission expense.

We incurred non-cash share-based compensation expenses related to SFAS No. 123(R) allocated to selling, general and administrative expenses in the six months ended March 31, 2009 and 2008 of \$964,952 and \$984,355, respectively.

We may expend additional resources on marketing and selling our products in future periods as we identify ways to optimize our potential opportunity. This may result in increased selling, general and administrative expenses in the future. Commission expense will also vary based on the sales channel and revenue levels.

#### ***Research and Development Expenses***

Research and development expenses decreased \$1,075,919 to \$901,108, or 11% of revenues, for the six months ended March 31, 2009, compared to \$1,977,027, or 43% of revenues, for the six months ended March 31, 2008. This decrease in research and development expense was primarily due to \$584,435 of higher consulting, prototypes and testing costs in the prior year for the development of our new LRAD-X product line. In addition, we had savings of \$293,706 from reduced staffing levels and \$129,777 from the reduction in expenses incurred for impairment of patents.

Included in research and development expenses for the six months ended March 31, 2009 and 2008 was \$78,988 and \$120,306 of SFAS No. 123(R) non-cash share-based compensation costs, respectively.

Each quarter, we review the ongoing value of our capitalized patent costs and in the first two quarters identified some of these assets as being associated with patents that are no longer consistent with our business strategy. As a result of this review, we reduced the value of our previously



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capitalized patents by \$75,744 during the six months ended March 31, 2009, compared to an impairment of \$205,521 in the six months ended March 31, 2008.

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Research and development costs vary period to period due to the timing of projects, the availability of funds for research and development and the timing and extent of use of outside consulting, design and development firms. We completed the development of the LRAD-X product line in the third fiscal quarter of 2008 with enhanced performance and louder, more intelligible communications. Based on current plans and reduced engineering staffing, we expect research and development costs to continue in the current fiscal year at a lower level than last year.

### ***Loss from Operations***

Loss from operations was \$26,857 for the six months ended March 31, 2009, compared to loss from operations of \$3,875,279 for the six months ended March 31, 2008. The decreased loss from operations is primarily attributable to the increase in revenues, improved gross profit margins and lower operating expenses.

### ***Other Income (Expense)***

During the six months ended March 31, 2009, we earned \$24,639 of interest income on our cash and cash equivalents balances compared to \$126,732 during the six months ended March 31, 2008 due to lower cash balances and lower interest rates. During the six months ended March 31, 2008, we recorded a \$108,821 financing expense for estimated liquidated damages based on certain registration rights agreements. We did not have a similar charge during the six months ended March 31, 2009.

### **Net Loss**

The net loss for the six months ended March 31, 2009 was \$2,218, a 100% decrease from a net loss of \$3,857,368 for the six months ended March 31, 2008. The significantly reduced loss was primarily the result of increased revenues, improved gross margins and lower operating expenses. We had no income tax expense for either of the periods presented.

### **Liquidity and Capital Resources**

We generated positive cash flow from operating activities and a net increase in cash and cash equivalents during the six months ended March 31, 2009 of \$204,212 and \$65,034, respectively. During this period, we financed our working capital requirements through cash and cash equivalents on hand at the beginning of the period, and from cash generated from operating activities. Cash and cash equivalents at March 31, 2009 was \$2,759,903 compared to \$2,694,869 at September 30, 2008. The net increase in cash and cash equivalents during this period resulted from net cash from operating activities, offset by \$139,178 in net cash used in investing activities that related to purchases of equipment and patent costs paid.

Other than cash and cash equivalents, inventory and our balance of accounts receivable, we have no other unused sources of liquidity as of March 31, 2009.

Principal factors that could affect the availability of our internally generated funds include:

ability to meet sales projections;

government spending levels;

introduction of competing technologies;

product mix and effect on margins;

ability to collect accounts receivable balances;

ability to reduce current inventory levels; and

product acceptance in new markets.

Principal factors that could affect our ability to obtain cash from external sources include:

volatility in the capital markets; and

market price and trading volume of our common stock.

Based on our current cash position and our order backlog, and assuming currently planned expenditures and level of operations, we believe we have sufficient capital to fund operations for the next twelve months. However, we operate in a rapidly evolving and unpredictable business environment that may change the timing or amount of expected future cash receipts and expenditures. Accordingly, there can be no assurance that we may not be required to raise additional funds through the sale of equity or debt securities or from credit facilities. Additional capital, if needed, may not be available on satisfactory terms, or at all.

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### ***Cash Flows***

#### ***Operating Activities***

Our net cash provided by operating activities was \$204,212 for the six months ended March 31, 2009 compared to cash used of \$1,749,948 from operating activities for the six months ended March 31, 2008. Net cash provided by operating activities for the six months ended March 31, 2009 included a \$2,218 net loss, decreased by expenses not requiring the use of cash of \$1,377,717, and \$289,426 in cash resulting from increased accounts payable. Operating cash usage during the six months ended March 31, 2009 included \$1,230,725 from increased accounts receivable, \$66,160 from decreased inventories, \$13,429 from increased prepaid expenses, \$11,513 for increased warranty settlements and \$138,886 decrease in accrued liabilities. Cash generated from operating activities for the six months ended March 31, 2008 included \$84,834 for decreased inventories, a \$676,786 increase in accounts payable and a \$668,656 increase in accrued liabilities. Cash used in operating activities for the six months ended March 31, 2008 included the \$3,857,368 net loss, reduced by expenses not requiring the use of cash of \$1,489,320, a \$733,541 increase in accounts receivable, a \$57,137 increase in prepaid expenses and a \$21,498 increase in warranty settlements.

At March 31, 2009 we had working capital of \$7,273,950, compared to working capital of \$6,105,286 at September 30, 2008.

At March 31, 2009, we had net accounts receivable of \$3,444,661, compared to \$2,210,526 in accounts receivable at September 30, 2008. The level of trade accounts receivable at March 31, 2009 represented approximately 53 days of revenue compared to approximately 72 days of revenue at September 30, 2008. Terms with individual customers vary greatly. We typically require thirty-day terms from our customers. Our receivables can vary significantly due to overall sales volumes and due to quarterly variations in sales and timing of shipments to and receipts from large customers and the timing of contract payments.

#### ***Investing Activities***

We use cash in investing activities primarily for the purchase of tooling, computer equipment and software and investment in new patents. Cash used in investing activities for equipment was \$118,048 for the six months ended March 31, 2009 and \$89,692 for the six months ended March 31, 2008. Cash used for investment in new patents was \$21,130 for the six months ended March 31, 2009 and \$117,766 for the six months ended March 31, 2008. We anticipate some additional expenditures for equipment and patents during the balance of fiscal year 2009.

#### ***Financing Activities***

There was no cash provided by or used in financing activities for the six months ended March 31, 2009 or 2008.

### **Recent Accounting Pronouncements**

A discussion of the new pronouncements can be found in Note 3 to our interim consolidated financial statements.

### **Item 3. Qualitative and Quantitative Disclosures about Market Risk.**

Not applicable.

### **Item 4. Controls and Procedures.**

We are required to maintain disclosure controls and procedures designed to ensure that material information related to us, including our consolidated subsidiaries, is recorded, processed, summarized and reported within the time periods specified in the SEC rules and forms.

### **Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures**

Under the supervision and with the participation of our management, including our principal executive officer and our principal financial officer, we conducted an evaluation of our disclosure controls and procedures, as such term is defined under Rules 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934. Based on this evaluation, our principal executive officer and our principal financial officer concluded that our disclosure controls and procedures were effective at the reasonable assurance level as of March 31, 2009.

**Changes in Internal Control over Financial Reporting**

There have been no changes in our internal control over financial reporting during our fiscal quarter ended March 31, 2009 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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Our process for evaluating controls and procedures is continuous and encompasses constant improvement of the design and effectiveness of established controls and procedures and the remediation of any deficiencies which may be identified during this process.

**PART II. OTHER INFORMATION****Item 1. Legal Proceedings.**

We may at times be involved in litigation in the ordinary course of business. We will also, from time to time, when appropriate in management's estimation, record adequate reserves in our financial statements for pending litigation. Currently, there are no pending material legal proceedings to which we are party or to which any of our property is subject.

**Item 1A. Risk Factors**

Not applicable.

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

None.

**Item 3. Defaults Upon Senior Securities.**

Not applicable.

**Item 4. Submission of Matters to a Vote of Security Holders.**

We held our Annual Meeting of Shareholders on March 25, 2009. The matters voted upon at the meeting included (a) the election of all five directors, and (b) ratification of the selection of Squar, Milner, Peterson, Miranda, & Williamson, LLP as the Company's independent registered public accounting firm for our fiscal year ending September 30, 2009. The votes cast with respect to these matters were as follows:

1. Election of Directors The following directors were elected at the meeting representing all of the directors of the Company:

| Nominee          | Number of shares<br>Voted For | Number of<br>shares Withheld |
|------------------|-------------------------------|------------------------------|
| Elwood G. Norris | 22,712,695                    | 1,722,387                    |
| Thomas R. Brown  | 22,763,341                    | 1,671,741                    |
| Daniel Hunter    | 23,888,327                    | 546,755                      |
| Raymond C. Smith | 23,860,648                    | 574,434                      |
| Laura M. Clague  | 23,880,367                    | 554,715                      |

2. Proposal to ratify the selection of Squar, Milner, Peterson, Miranda, & Williamson, LLP as our independent registered public accounting firm for our fiscal year ending September 30, 2009.

For

Against

Abstain

Broker - No Vote

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23,786,511

449,496

199,075

**Item 5. Other Information.**

None

**Item 6. Exhibits**

- 31.1 Certification of Thomas R. Brown, Principal Executive Officer, pursuant to Rule 13a-14(a) or 15d-14(a) of the Securities and Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of Katherine H. McDermott, Principal Financial Officer, pursuant to Rule 13a-14(a) or 15d-14(a) of the Securities and Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, executed by Thomas R. Brown, Principal Executive Officer and Katherine H. McDermott, Principal Financial Officer.

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99.1 Press release dated April 29, 2009 regarding fiscal Q2 2009 financial results. (This exhibit has been furnished and shall not be deemed filed for purposes of Section 18 of the Securities Exchange Act of 1934, nor shall it be deemed incorporated by reference in any filing under the Securities Act of 1933, except as shall be expressly set forth by specific reference in such filing.)

**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.

AMERICAN TECHNOLOGY CORPORATION

Date: April 29, 2009

By: */s/ Katherine H. McDermott*  
**Katherine H. McDermott, Chief Financial Officer**

**(Principal Financial Officer)**