DYNATEC INTERNATIONAL INC
Form 10QSB
May 15, 2001

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

FORM 10-QSB

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

For the Quarterly Period Ended: March 31, 2001

[ ] 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: 0-12806

DYNATEC INTERNATIONAL, INC.
(Exact name of small business issuer as specified in its charter)

UTAH	87-0367267
(State or other jurisdiction of incorporation or organization)	(IRS employer identification no.)

3820 Great Lakes Drive Salt Lake City, Utah	84120
(Address of principal executive offices)	(Zip Code)

(801) 973-9500
(Issuer's telephone number, including area code)

N/A
(Former name, former address and former fiscal year, if changed since last report)

Check whether the issuer (1) 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. X Yes No

The Company had 5,745,640 shares of common stock outstanding at May 2, 2001.

The aggregate market value of voting stock held by non-affiliates of the Company at May 2, 2001 was $492,050.

Transitional small business disclosure format. ------ Yes X No

DYNATEC INTERNATIONAL, INC. AND SUBSIDIARIES

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PART I - FINANCIAL INFORMATION

ITEM 1. Financial Statements

DYNATEC INTERNATIONAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

ASSETS

	March 31, 20
	(Unaudited)
CURRENT ASSETS:	
Cash and cash equivalents	$ 12,04
Trade accounts receivable, net of allowance for doubtful accounts of $54,297 and $56,800, at March 31, 2001 and December 31, 2000 respectively	1,092,28
Inventories (note 2)	1,047,10
Prepaid expenses and other	96,15
Net assets of discontinued operations	
Total current assets	2,247,59
PROPERTY AND EQUIPMENT, at cost:	
Building and improvements	2,865,00
Furniture, fixtures, and equipment	2,976,58
	5,841,58
Less accumulated depreciation and amortization	2,394,03
Net property and equipment	3,447,55
GOODWILL AND OTHER IDENTIFIABLE INTANGIBLES, net (note 2)	141,7
DEFERRED LOAN COSTS, net of accumulated amortization of $62,388 and $56,001, respectively	4,2
OTHER ASSETS	72,6
	$ 5,913,8

See accompanying notes to condensed consolidated financial statements.

DYNATEC INTERNATIONAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS (continued)

LIABILITIES AND STOCKHOLDERS' EQUITY

	March 31, 2
	(Unaudited
CURRENT LIABILITIES:	
Short-term note payable	$ 475,
Current portion of long-term debt	60,
Current portion of capital lease obligations	73,
Accounts payable	1,340,
Note payable-related party	150,
Accrued expenses	560,
Accrued advertising	239,
Accrued royalties payable	138,
Net liabilities of discontinued operations	21,
Total current liabilities	3,059,
DEFERRED GAIN ON SALE OF ASSET	228,
CAPITAL LEASE OBLIGATIONS, net of current portion	2,870,
Total liabilities	6,158,
STOCKHOLDERS' EQUITY :	
Common stock, $.01 par value; 100,000,000 shares authorized and 5,745,640 shares outstanding at March 31, 2001 and December 31, 1999	57,
Additional paid-in capital	10,320,
Accumulated deficit	(10,622,
Net stockholders' (deficit) equity	(244,
COMMITMENTS AND CONTINGENCIES	
	$ 5,913,

See accompanying notes to condensed consolidated financial statements.

DYNATEC INTERNATIONAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Three months ended March 31, 2001
	(Unaudited)
PRODUCT SALES	1,942,632
COST OF SALES	(981,427)
Gross Margin	961,205
OPERATING COSTS AND EXPENSES:	
Selling expenses	599,791
General and administrative	576,488
Research and development	-
Total operating costs and expenses	1,176,279
Operating loss from continuing operations	(215,074)
OTHER INCOME (EXPENSE):	
Interest expense	(126,051)
Equity in loss of affiliate (note 4)	(19,477)
Other income	60
Total other expense, net	(145,468)
Loss from continuing operations before income tax benefit	(360,542)
INCOME TAX BENEFIT	-
Loss from continuing operations	(360,542)
DISCONTINUED OPERATIONS:	
Income from operations of discontinued home storage and organization segment net of income tax	-

Net loss	$ (360,542)
LOSS PER SHARE FROM CONTINUING OPERATIONS- BASIC AND DILUTED	$ (.06)
EARNINGS PER SHARE FROM DISCONTINUED OPERATIONS- BASIC AND DILUTED	$ -
NET LOSS PER SHARE- BASIC AND DILUTED	$ (.06)
WEIGHTED AVERAGE SHARES - BASIC AND DILUTED	5,745,640

See accompanying notes to condensed consolidated financial statements.

DYNATEC INTERNATIONAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Three months ende March 31, 2001
CASH FLOWS FROM OPERATING ACTIVITIES:	(Unaudited)
Net loss	$ (360,542)
Net income from discontinued operations	-
Adjustments to reconcile net loss to net cash used in operating activities:	
Depreciation and amortization	128,346
Amortization of deferred loan costs	6,387
Amortization of deferred gain on sale of assets	(3,081)
Forgiveness of liquidated damages related to convertible debenture (note 4)	-
Gain on sale of assets	(60)
Provision for losses on accounts receivable	(2,503)
Changes in operating assets and liabilities:	
Trade accounts receivable	(283,362)
Inventories	203,946
Prepaid expenses	4,939
Other assets	19,364
Accounts payable	(29,481)
Accrued expenses	527
Accrued advertising	(125,934)
Accrued royalties	33,338

Net cash used in continuing operating activities	(408,116)
Net cash provided by discontinued operating activities	200,063
Net cash used in operating activities	(208,053)
CASH FLOWS FROM INVESTING ACTIVITIES:	
Net proceeds from the sale of assets	200
Purchase of property and equipment	(12,366)
Net cash used in continuing investing activities	(12,166)
Net cash used in discontinued investing activities	-
Net cash used in investing activities	(12,166)
CASH FLOWS FROM FINANCING ACTIVITIES:	
Net borrowings (payments) on line of credit	(9,664)
Net payments on long-term debt	(20,625)
Net principal payments on capital lease obligations	(15,981)
Net proceeds from related party note payable	150,000
Payment to retire convertible debenture	-
Proceeds from the issuance of common stock related to private placement	-
Net cash provided by continuing financing activities	103,730
Net cash used in provided by discontinued financing activities	-
Net cash provided by financing activities	103,730
NET DECREASE IN CASH AND CASH EQUIVALENTS	(116,489)
CASH AND CASH EQUIVALENTS AT BEGINNING OF THE PERIOD	128,536
CASH AND CASH EQUIVALENTS AT END OF THE PERIOD	$ 12,047

See accompanying notes to condensed consolidated financial statements.

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DYNATEC INTERNATIONAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)

	Three months ended March 31, 2001 (Unaudited)
SUPPLEMENTAL SCHEDULE OF CASH FLOW INFORMATION:	

Cash paid for interest	$ 123,793
SUPPLEMENTAL SCHEDULE OF NONCASH INVESTING AND FINANCING ACTIVITIES:	
Property and equipment acquired under capital leases	-
Conversion of Convertible Debentures and accrued interest for common stock	-

See accompanying notes to condensed consolidated financial statements.

DYNATEC INTERNATIONAL, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(1) DESCRIPTION OF BUSINESS AND NATURE OF OPERATIONS

Dynatec International, Inc., a Utah corporation ("Dynatec" or the "Company"), is a manufacturer and distributor of consumer products in the following major product lines: telecommunication headsets and amplifiers and telephone accessories, and flashlights. Dynatec is located in Salt Lake City, Utah. The Company conducts most of its operations through its wholly owned subsidiaries: Softalk, Inc., SofTalk Communications, Inc., Arnco Marketing, Inc., and Nordic Technologies, Inc. Unless specified to the contrary herein, references to Dynatec or to the Company refer to the Company and its subsidiaries on a consolidated basis.

The Company's business follows seasonal trends. As a result the Company experiences its highest revenues in the fourth quarter. Because the Company sells its products primarily to major retailers, the Company's sales performance is significantly dependent on the performance of those retailers.

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared by the Company in accordance with the rules and regulations of the Securities and Exchange Commission for Form 10-QSB, and accordingly, do not include all of the information and footnotes required by generally accepted accounting principles. In the opinion of management, these unaudited condensed consolidated financial statements reflect all adjustments, which consist only of normal recurring adjustments, which are necessary to present fairly the Company's financial position, results of operations and cash flows as of March 31, 2001, and for the periods presented herein. These unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-KSB for the year ended December 31, 2000.

The results of operations for the three months ended March 31, 2001 are not necessarily indicative of the results that may be expected for the remainder of the year ending December 31, 2001.

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Inventories

Inventories, consisting principally of telecommunication headsets and amplifiers and telephone accessories, flashlights, and other miscellaneous products as of March 31, 2001 and December 31, 2000, respectively, are summarized as follows:

	March 31, 2001	December 31, 2000
Raw materials...........................	$ 333,308	$423,667
Work-in-Process.........................	61,911	65,390
Finished Goods..........................	651,887	761,995
	$1,047,106	$1,251,052

Basic and Diluted Net Income (Loss) Per Common Share

Basic net loss per common share is calculated based upon the weighted average number of common shares outstanding during the periods presented. Diluted loss per common share is the amount of loss for the period for each share of common stock outstanding during the reporting period and for each share that would have been outstanding assuming the issuance of common shares for all dilutive potential common shares outstanding during the period.

In calculating net loss per share for the three months ended March 31, 2001, and 2000, warrants and options to purchase 593,250 and 775,750 potential common shares, respectively, are not included in the computation of diluted

net loss per common share as their effect would have been anti-dilutive, thereby decreasing the net loss per common share.

Goodwill

Goodwill represents the excess of the purchase price over the fair value of the net assets acquired from Transworld Products, Inc. (Transworld) on July 15, 1999. The goodwill is being amortized using the straight-line basis over two years. The balance as of March 31, 2001 and December 31, 2000 was as follows:

	2001	2000
Goodwill	$ 34,306	$ 34,306
Accumulated amortization	27,873	25,729
	$ 6,433	$ 8,577

(3) BUSINESS SEGMENT INFORMATION

Information as to the operations of the Company in different business segments is set forth below based on the nature of the products and services offered. Management evaluates performance based on several factors, of which the primary financial measure is business segment operating income before non-cash amortization of intangible assets ("EBITDA"). The accounting policies of the business segments are the same as those described in the summary of significant accounting policies.

	THREE MONTHS ENDED MARCH 31,	
REVENUES:	2001	2000
Telecommunication Headsets and		
Amplifiers and Telephone Accessories..........	$ 1,714,000	$ 1,866,000
Flashlights....................................	201,000	588,000
Hardware/Houseware.............................	28,000	197,000
Total....................................	$ 1,943,000	$ 2,651,000

	THREE MONTHS ENDED MARCH 31,	
OPERATING INCOME (LOSS):	2001	2000
Telecommunication Headsets and		
Amplifiers and Telephone Accessories..........	$ (64,000)	$ (137,000)
Flashlights....................................	(137,000)	(412,000)
Hardware/Houseware.............................	(14,000)	(52,000)
	$ (215,000)	$ (601,000)

(3) BUSINESS SEGMENT INFORMATION (Continued)

	THREE MONTHS ENDED MARCH 31,	
DEPRECIATION AND AMORTIZATION (1):	2001	2000
Telecommunication Headsets and		
Amplifiers and Telephone Accessories..........	$ 113,000	$ 103,000
Flashlights....................................	14,000	32,000
Hardware/Houseware.............................	1,000	11,000

Miscellaneous/Mass Market	-	-
Total	$ 128,000	$ 146,000

(1) Amortization includes all amortization relating to goodwill, product license rights, non-competes and purchased patents.

Information as to the assets and capital expenditures of Dynatec International, Inc. is as follow

ASSETS:	MARCH 31, 2001	DECEMBER 31, 2000
Telecommunication Headsets and Amplifiers and Telephone Accessories	$ 4,945,000	$ 4,098,000
Flashlights	682,000	1,111,000
Hardware/Houseware	102,000	554,000
Discontinued operations	-	179,000
Total assets for reportable segments	5,729,000	5,942,000
Other assets	73,000	92,000
Deferred loan costs and other assets not allocated to segments	112,000	240,000
Consolidated total	$ 5,914,000	$ 6,274,000

	THREE MONTHS ENDED MARCH 31,	
CAPITAL EXPENDITURES:	2001	2000
Telecommunication Headsets and Amplifiers and Telephone Accessories	$ 12,000	$ 72,000
Flashlights	-	21,000
Hardware/Houseware	$ -	5,000
Total	$ 12,000	$ 98,000

Information as to Dynatec International, Inc.'s operations in different geographical areas is as follows:

	THREE MONTHS ENDED MARCH 31,	
REVENUES:	2001	2000

United States..........................	$ 1,935,000	$ 2,543,000
Other (1).............................	8,000	108,000
Total..........................	$ 1,943,000	$ 2,651,000

(1) Includes Canada, Europe, and other miscellaneous.

(3) BUSINESS SEGMENT INFORMATION (Continued)

	THREE MONTHS ENDED MARCH 31,	
OPERATING LOSS:	2001	2000
United States.......................	$ (215,000)	$ (601,000)

ASSETS:	MARCH 31, 2001	DECEMBER 31, 2000
United States.......................	$ 5,638,000	$ 5,978,000
Asia................................	276,000	296,000
Total........................	$ 5,914,000	$ 6,274,000

(4) JOINT VENTURE

In January 2001, the Company's Nordic Technologies, Inc. subsidiary ("Nordic") formed a joint venture called Nordic ASI, L.L.C. that is owned 50% by Nordic and 50% by Sarkat International, L.L.C., a Utah limited liability company that is owned, in part, by Reed Newbold, who is a member of the Company's board of directors. Nordic ASI was formed specifically to enable the Company to pursue sales of its flashlight product line (and other flashlights and products not then offered by the Company) in the advertising, specialty and promotional market (the "ASI Market"). Prior to the formation of Nordic ASI, the Company was not engaged directly in the ASI Market, although until the end of 2000, it was a supplier of flashlight products to one or more companies that sell in the ASI Market. As its capital contribution, the Company contributed rights to sell its products in the ASI Market to Nordic ASI, and agreed to incur the administrative expense associated with operating Nordic ASI and marketing its products for a period of two years. For its capital contribution, Sarkat agreed to provide $200,000 of debt financing to Nordic ASI to enable it to start up its operations. Profits and losses of Nordic ASI will be allocated 70% to Nordic and 30% to Sarkat. Nordic ASI obtained the $200,000 of debt financing provided by Sarkat and has commenced its business of selling to the ASI Market by ordering

LED flashlights provided by an unaffiliated third party. The Company believes that, given its current financial condition, it could not have commenced any sales effort in the ASI Market or supplemented its product line for that market absent the formation of the joint venture with Sarkat.

(5) GOING CONCERN

Based on current operations, the Company believes that its present sources of liquidity will not be adequate to meet its projected requirements for working capital, capital expenditures, scheduled debt service requirements and other general corporate purposes for the remainder of the year 2001. The Company is currently pursuing additional sources of liquidity in the form of traditional commercial credit, asset based lending or additional sales of the Company's debt or equity securities to finance its ongoing operations. Additionally, the Company has entered into interim financing transactions, including $150,000 of revolving unsecured credit provided by an entity affiliated with a member of the Company's board of directors. The Company also is pursuing other, types of commercial and private financing which could involve sales of substantial portions of the Company's accounts receivable, sales of the Company's assets or sales of one or more operating divisions. The Company's sales have been adversely affected by the Company's reduced credit availability and lack of access to other financing because of its reduced ability to purchase product to fill existing orders. If additional financing is not obtained in the near future, the Company will be required to more significantly curtail its operations or seek protection under bankruptcy laws.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

Results of Operations

The following table sets forth, for the periods indicated, certain information relating to the operations of the Company expressed in dollars (rounded) and percentage changes from period to period. Data in the table reflects the consolidated results of the Company for the three months ended March 31, 2001 and 2000, respectively. As supplemental information, the table also segregates the Company's revenues by product line type.

	(ROUNDED) For the Three Months Ended		
	MARCH 31, 2001	MARCH 31, 2000	%OF CHG FROM 2000 TO 2001
Unaudited Statement of Operations Data:			
Product sales............	$1,943,000	$2,651,000	(26.7)%
Cost of sales............	982,000	1,444,000	(32.0)

Gross margin......	961,000	1,207,000	(20.4)
Operating Costs and Expenses:			
Selling expenses..........	600,000	915,000	(34.4)
General and administrative	576,000	798,000	(27.8)
Research and development..	-	95,000	(100.0)
Total operating costs and expenses..........	1,176,000	1,808,000	(35.0)
Other Income (Expense), net:			
Interest expense..........	(127,000)	(135,000)	(5.9)
Equity in loss of affiliate.................	(19,000)	-	-
Other income..............	-	2,000	(100.0)
Total other income (expense)..................	(146,000)	(133,000)	9.8
Loss from continuing operations................	(361,000)	(734,000)	(50.8)
Discontinued Operations:			
Income from discontinued operations	-	225,000	(100.0)
Net loss..................	$ (361,000)	$ (509,000)	(29.1)
Unaudited Supplemental Information:			
Revenue by product line type:			
Telecommunication headsets and amplifiers and telephone accessories.......	$ 1,714,000	$ 1,866,000	(8.1)
Flashlights..................	201,000	588,000	(65.8)
Hardware/houseware...........	28,000	197,000	(85.8)
Total product sales and other..........	$1,943,000	$ 2,651,000	(26.7)

Following are explanations of significant period-to-period changes for the three months ended March 31, 2001 and 2000:

Revenues

Total Product Sales. Total product sales decreased by $708,000, or 26.7%, from $2,651,000 to $1,943,000 for the three months ended March 31, 2001 compared to the three months ended March 31, 2000.

Telecommunication Headsets and Amplifiers and Telephone Accessories. Telecommunication headsets and amplifiers and telephone accessories sales decreased $152,000, or 8.1%, from $1,866,000 to $1,714,000 for the three months

ended March 31, 2001 compared to the three months ended March 31, 2000. This decrease is primarily related to decreases in sales of the Company's shoulder rest products of $251,000, and telephone headsets and amplifiers of $162,000. These sales decreases were partially attributable to the Company's inability to acquire product to fill existing orders because of decreased credit availability and a lack of alternate capital resources. The decrease was offset in part by an increase of $202,000 in the Company's Twisstop products and $59,000 in other telephone accessory products. Overall gross margins for this product line decreased to 53.7% from 57.4% for the three months ended March 31, 2001 compared to the three months ended March 31, 2000, as a result of the sales mix.

Flashlights. Flashlight revenues decreased $387,000, or 65.8% from $588,000 to $201,000 for the three months ended March 31, 2001 compared to the three months ended March 31, 2000. This decrease was primarily the result of the company's decision to move its flashlight manufacturing to a different Asian supplier causing some short term delays in the delivery of product and to the Company's decreased credit availability and lack of alternate capital resources. Overall gross margins for products in this category increased from 14.9% to 18.6% for the three months ended March 31, 2001 when compared to March 31, 2000, as a result of a decrease in material costs of the products due to a change in the manufacturer.

Houseware/Hardware. Houseware/hardware revenues decreased $169,000, or 85.8%, from $197,000 to $28,000 for the three months ended March 31, 2001 compared to the three months ended March 31, 2000. The decrease is primarily attributable to the loss of the Company's main customer in the doorstops product line as a result of an increase in the Company's pricing. Overall gross margins for products in this category increased from 24.8% to 40.3% for the three months ended March 31, 2001 compared to March 31, 2000, as a result of the increase in pricing.

Operating Costs and Expenses

Selling Expenses. Selling expenses decreased $315,000, or 34.4%, from $915,000 to $600,000 for the three months ended March 31, 2001 compared to the three months ended March 31, 2000. This decrease is due in part to a decrease in salaries for sales personnel of $61,000 due to a reduction in force of the sales support staff, as well as decreases in commissions paid to outside sales representatives of $65,000, travel related expenses of $48,000, consulting fees of $47,000, freight expenses of $45,000 and royalties of $21,000.

General and Administrative Expenses. General and administrative expenses decreased $222,000, or 27.8%, from $798,000 to $576,000 for the three months ended March 31, 2001 compared to the three months ended March 31, 2000. The decrease in general and administrative expenses was primarily the result of a decrease of $50,000 in salaries paid as a result of the Company's August 11, 2000 reduction in force, as well as a decrease in legal and accounting fees of $52,000, consulting fees of $41,000, office and computer supplies of $25,000, employee recruitment and education expenses of $19,000, and a decrease of $18,000 in travel related expenses.

Research and Development. Research and development expenses decreased by $95,000, from $95,000 to -0- for the three months ended March 31, 2001

compared to the three months ended March 31, 2000. The decrease was primarily attributable to the completion in 2000 of the Company's research and development efforts associated with the Company's flashlight line to improve the function and appearance of the products.

Total Operating Costs and Expenses. Total operating costs and expenses decreased by $632,000, or 35.0%, from $1,808,000 to $1,176,000 for the three months ended March 31, 2001 compared to the three months ended March 31, 2000, for the reasons discussed above.

Interest Expense. Interest expense decreased $8,000, or 5.9%, from $135,000 to $127,000 for the three months ended March 31, 2001 compared to the three months ended March 31, 2000. This decrease is primarily the result of the Company's reduction in interest expenses related to its revolving credit facility. These decreases were offset in part by an increase in interest expense related to the Company's joint venture and financing arrangement with Sarkat International, LLC (see note 4 to the condensed consolidated financial statements).

Equity in loss of affiliate. Equity in loss of affiliate decreased by $19,000 from -0- to $(19,000) for the three months ended March 31, 2001 compared to the three months ended March 31, 2000. This decrease is attributable to the Company's joint venture with Sarkat International, LLC (see note 4 to the condensed consolidated financial statements).

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Other Income/expense. Other income (expense) decreased $2,000, from $2,000 to -0- for the three months ended March 31, 2001 compared to the three months ended March 31, 2000. The decrease is due to a gain on sale of assets of $2,000 that occurred in the three months ended March 31, 2000.

Discontinued operations. Income from discontinued operations decreased $225,000 from $225,000 to -0 for the three months ended March 31, 2001 compared to the three months ended March 31, 2000. This decrease is attributable to the sale of the assets of the Company's Neat Things! (TM) home organization and storage product line in November 2000.

Net loss. The net loss decreased by $148,000, or 29.1%, from a loss of $509,000 to a loss of $361,000 for the three months ended March 31, 2001 compared to the three months ended March 31, 2000 due to a combination of the factors described above.

Liquidity and Capital Resources

General

The Company's principal sources of liquidity historically have been cash flows from operations, cash on hand and borrowing under the Company's existing secured revolving credit facility. On May 27, 1998, the Company obtained its secured revolving credit facility from a regional financing institution for up to $5,000,000, bearing interest at a rate of prime plus one percent, with interest payable monthly. In previous amendments to the credit agreement the maximum line was decreased to $2,200,000 and the interest rate was increased to a rate of prime plus five percent. The Company's assets, including accounts receivable and inventories, secure the credit facility. The note underlying the revolving credit line is due May 26, 2001. On April 5, 2001 the Company and its lending institution entered into a Tenth Amendment to the Credit Agreement (the "Tenth Amendment"). Pursuant to this amendment the maximum line decreased from $2,200,000 to $600,000. Notwithstanding the extent of the maximum borrowing under the note, the covenants of the agreement limit the Company's

borrowing availability based on percentages of current inventory and accounts receivable. Under the terms of the loan agreement, the Company is required to maintain financial covenants and ratios, including book net worth, net income and debt service coverage. As of March 31, 2001 the Company was in default of certain of these financial covenants. Although the Company's secured lender has not indicated its intention to accelerate payment of the outstanding balance payable under the note because of such defaults, it has informed the Company will not extend the payment deadline for the note, nor will the lender extend additional credit to the Company. The Company is therefore attempting to locate an alternate source of commercial lending.

In February 2001, and due to decreases in the Company's operating capital and borrowing availability, the Company entered into a relationship with Sarkat International, LLC ("Sarkat"), a limited liability company that is owned in part by Reed Newbold, who currently is a member of the Company's board of directors. In connection with this arrangement, Sarkat agreed to provide unsecured, revolving debt financing to Softalk, Inc. or Softalk Communications, Inc., each a subsidiary of the Company, in the aggregate amount of $150,000. In exchange for each advance of funds by Sarkat, the Company (or its subsidiary directly receiving such funds) is obligated to repay the principal amount advanced, plus interest calculated on a daily basis at the annual rate of the greater of eight and one-half percent or the actual rate of interest paid by Sarkat to obtain such funds, plus a "lender's premium" of 12.5% of the principal amount advanced. Such borrowed funds are disbursed by direct payment by Sarkat to the Company's supplier, who then ships product to the Company, which allows the Company to service pending orders from its customers. Principal, interest and lender's premiums payable to Sarkat, to the extent paid, have been repaid out of loan advances from the Company's secured lender when the Company's accounts receivable borrowing base increases as result of the sales facilitated by the Sarkat loans. The Company's secured lender has consented to this mechanism. As of May 2, 2001, the Company owes Sarkat $150,000 in principal $2,493 in interest and $5,625 in lenders premium. Sarkat has been paid $27,619 in lender's premiums. The principal and interest are due 180 days from the date of the advance. Debt financing on similar or terms more preferential to the Company was not available to the Company at the time.

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March 31, 2001 Compared to December 31, 2000

As of March 31, 2001 the Company had liquid assets (cash and cash equivalents and trade accounts receivable) of $1,104,000, an increase of 18.1%, or $169,000, from December 31, 2000 when liquid assets were $935,000. Cash decreased $116,000, or 90.6%, to $12,000 at March 31, 2001 from $128,000 at December 31, 2000. The decrease in cash was primarily the result of the Company utilizing its revolving credit facility, under which "draws" are made by the Company to fund capital expenditures, purchase inventory and for general-purpose use. After a draw is made a corresponding payable is setup, when collections of outstanding accounts receivable are made the monies collected, are swept, the next day, and re-applied against outstanding draws. Trade accounts receivable increased $286,000, or 35.5%, to $1,092,000 at March 31, 2001 from $806,000 at December 31, 2000. This increase is primarily the result of increased sales in March 2001.

Current assets decreased by $218,000, or 8.8%, to $2,248,000 at March 31, 2001 from $2,466,000 at December 31, 2000. This decrease was primarily the result of a decrease in cash of $116,000, discussed above, a decrease in inventory by $204,000 primarily due to the Company's efforts to reduce inventory levels to a one month's supply, and a decrease in net assets of discontinued

operations of $179,000 due to the sale of the assets of the Company's Neat Things! (TM) home organization and storage product line. The decrease in current assets was offset in part by an increase in trade accounts receivable, as discussed above.

Long-term assets decreased $142,000, or 3.7%, to $3,666,000 at March 31, 2001 from $3,808,000 at December 31, 2000. This decrease was primarily the result of recurring depreciation expense on property and equipment, and amortization of deferred loan costs, and other intangibles.

Current liabilities increased by $21,000, or 0.7%, to $3,059,000 at March 31, 2001 from $3,038,000 at December 31, 2000. This increase was primarily due to an increase of $150,000 in note payable-related party as a result of the Company's February 2001 agreement with Sarkat, and an increase in accrued royalties of $54,000. These increases were offset in part by a decrease in accrued advertising of $126,000, trade accounts payable of $29,000 and the current portion of long term debt of $21,000.

The Company's working capital deficit increased by $239,000, or 41.8%, to ($811,000) at March 31, 2001 from ($572,000) at December 31, 2000, for the reasons described above.

The Company used cash of $408,000 from continuing operating activities during the three months ended March 31, 2001, primarily from the net loss incurred during the period, an increase in trade accounts receivable and a decrease in accrued advertising, offset in part by decreased inventory levels.

The Company used net cash of $12,000 in investing activities during the three months ended March 31, 2000, primarily for capital expenditures for property and equipment.

The Company provided net cash of $104,000 from financing activities during the three months ended March 31, 2001 primarily as a result of the proceeds from the related party note payable, offset in part by payments made on the Company's revolving line-of-credit, long-term debt and capital lease obligations during the period.

Based on current operations, the Company believes that its present sources of liquidity will not be adequate to meet its projected requirements for working capital, capital expenditures, scheduled debt service requirements and other general corporate purposes for the remainder of the year 2001. The Company is currently pursuing additional sources of liquidity in the form of traditional commercial credit, asset based lending or additional sales of the Company's debt or equity securities to finance its ongoing operations. Additionally, the Company has entered into interim financing transactions, including $150,000 of revolving unsecured credit provided by an entity affiliated with a member of the Company's board of directors. The Company also is pursuing other types of commercial and private financing which could involve sales of substantial portions of the Company's accounts receivable, sales of the Company's assets or sales of one or more operating divisions. The Company's sales and financial condition have been adversely affected by the Company's reduced credit availability and lack of access to alternate financing because of its reduced ability to purchase product to fill existing orders. If additional financing is not obtained in the near future, the Company will be required to more significantly curtail its operations or seek protection under bankruptcy laws.

Seasonality

The Company's business is seasonal. The Company typically experiences its highest sales volume in the fourth quarter of each year as a result of the retail environment in which most of its customers conduct business. Because the Company sells its products primarily to major retailers, the Company's sales performance is significantly dependent on the performance of those retailers. Accordingly, the fourth quarter is a key determinate to overall profitability for the year.

Forward Looking Statements

The foregoing Management's Discussion and Analysis of Financial Condition and Results of Operations contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, which are intended to be covered by the safe harbors created thereby. Although the Company believes that the assumptions underlying the forward-looking statements contained herein are reasonable, any of the assumptions could be inaccurate, and therefore, there can be no assurance that the forward-looking statements will prove to be accurate. Factors that could cause actual results to differ from results discussed in forward-looking statements include, but are not limited to, potential increases in inventory costs, competition, the Company's ability to obtain additional working capital to fund future growth and any of the risks described in the Company's Annual Report on Form 10-KSB for the year ended December 31, 2000.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

On February 8, 2001, the Company waived service of a summons with respect to a complaint filed in the U.S. District court in the District of Utah by K&S Flashlight, Inc. ("K&S"), a Taiwan company that was the Company's flashlight supplier from 1998 through 2000. The lawsuit names as defendants both Dynatec and its subsidiary, Nordic Technologies, Inc. The lawsuit alleges that the Company owes K&S in excess of $100,000 for the Company's alleged failure to pay amounts due to K&S for flashlight products shipped during 2000, and seeks damages in an unspecified amount. The Company has filed its answer and intends to vigorously defend the lawsuit.

On August 4, 2000, the Company filed suit (the "Utah WAC Action") against WAC Research, Inc., a Utah corporation ("WAC"), in Utah state court in Salt Lake City, Utah. WAC is a corporation at least fifty percent of which is owned by Donald M. Wood ("Wood"), the Company's former Chairman and Chief Executive Officer. The dispute with WAC arose out of a series of royalty agreements between the Company and WAC dated in 1990 and 1998 that purported to obligate the Company to pay perpetual royalties to WAC on sales of products in the Company's telephone accessories product line. In return for this perpetual royalty (which the Company paid for approximately 10 years) WAC purported to assign and grant to the Company the intellectual property rights underlying certain of the Company's Softalk products. At the times the WAC agreements were negotiated, Wood controlled both WAC and the Company. The Company amended its complaint in the Utah WAC Action on August 29, 2000 and on October 19, 2000. After the Company was unable to negotiate a settlement of its disputes with WAC, and after WAC filed its own complaint in state court in Phoenix, Arizona (the

"Arizona WAC Action") on October 6, 2000, the Company served process in the Utah WAC Action. The Company's complaint in the Utah WAC Action, as amended to date, seeks the court's declaration that no further royalties are owed by the Company to WAC because, among other reasons, (i) WAC never had any interest in or to any of the intellectual property rights underlying the Company's Softalk products, (ii) WAC breached its representations and warranties of ownership as to such intellectual property rights as set forth in the WAC agreements, (iii) patents covering certain of the key products in the Company's Softalk product line have expired, and such products are not otherwise covered by enforceable copyrights or other intellectual property rights, (iv) the Company owns all trademark rights with respect to its Softalk products, (v) WAC has no right to continue forcing the Company to pay royalties under expired patents, (vi) WAC's ongoing attempts to enforce the WAC royalty agreements constitute patent misuse, and (vii) as a consequence of WAC's patent misuse, WAC is liable to the Company for royalties paid under a 1998 agreement between WAC and the Company. The complaint in the Utah WAC Action also includes claims for damages stemming from WAC's alleged patent misuse, failure of consideration, unjust enrichment and additional declaratory relief. WAC's complaint in the Arizona WAC Action alleges that WAC made unspecified loans to the Company that were never repaid, and that the Company is in breach of its royalty payment obligations under the WAC royalty agreements. In the Arizona WAC Action, WAC sought declaratory judgment that the Company is required prospectively to pay royalties under the WAC agreements and for money damages in the amount of $308,841. The Company moved to dismiss the Arizona WAC Action for lack of jurisdiction or, in the alternative to stay the Arizona WAC Action pending a resolution of the Utah WAC Action. On February 26, 2001, the court in the Arizona WAC Action granted the Company's motion to dismiss that action. On March 27, 2001, WAC filed a counterclaim against the Company in the Utah WAC Action. This counterclaim asserts claims that are identical to those that were asserted by WAC in the Arizona WAC Action before it was dismissed. The Utah WAC Action is still pending, and the Company intends to vigorously prosecute it.

In February 1999, Mag Instrument, Inc., a manufacturer and distributor of flashlights and one of the Company's competitors ("Mag"), filed a lawsuit against the Company's subsidiary, Nordic Technologies, Inc. ("Nordic"), of infringing certain of Mag's patents and committing false advertising and unfair competition. The lawsuit was filed in the U.S. District Court for the Central District of California. The Company and Mag attempted to settle that lawsuit, and entered into an agreement whereby the lawsuit was dismissed without prejudice, with Mag having the express right to refile the complaint in the same court and venue. No settlement was ever reached. On October 30, 2000, Mag filed

a new complaint in the same federal district court that it subsequently served on the Company. The new Mag complaint alleges that Nordic has infringed two patents and related trademarks owned by Mag, and also has engaged in unfair competition arising out of Nordic's alleged use of a flashlight design that is confusingly similar to the shape, style and overall appearance of Mag's miniature "AA" light, all in violation of various provisions of federal and California state law. Mag seeks unspecified money damages, punitive damages and injunctive relief. The Company does not believe that any of Nordic's flashlight products have infringed any patents or trademarks of Mag, and intends to vigorously defend the suit.

On May 4, 2000, Grandur, Inc., a Taiwan corporation ("Grandur"), sued the Company in the United States District Court for the District of New Jersey. The summons and complaint were served on the Company in Salt Lake City, Utah on May 12, 2000. The complaint alleges that the Company has breached a manufacturing agreement between the Company and Grandur pursuant to which the

Company is alleged to have a minimum annual purchase requirement and an exclusive manufacturing arrangement with Grandur for the Company's Twisstop product. The complaint further alleges that Grandur is entitled to recover, in addition to such damages as may be proved at trial, liquidated damages per the terms of the contract in the amount of $500,000. Grandur and the Company have entered into an oral agreement to settle this litigation and are making efforts to memorialize their agreement. On February 6, 2001, Grandur and the Company reported the terms as their settlement to the court. On February 7, 2001, the court entered an order conditionally dismissing the lawsuit subject to being reopened if the settlement is not consummated. In the event the settlement is not consummated, the Company intends to vigorously defend the lawsuit.

In February 2000, Merrill Lynch & Co., Inc. ("Merrill Lynch") notified the Company that American Stock Transfer & Trust Co., New York, New York, the Company's stock transfer agent ("AST"), had confiscated three separate certificates purporting to represent a total of 208,000 shares of restricted common stock issued in the name of an entity affiliated with Donald M. Wood, the Company's former Chairman and Chief Executive Officer. AST confiscated such certificates because they were not then shown as valid certificates representing the Company's issued and outstanding common stock. Based on further investigation by AST, the Company believes that its former stock transfer agent had transferred the shares represented by such certificates to third parties, but had not received the original certificates representing such shares at the time of those transfers. Nor did the former transfer agent obtain documentation indicating that such certificates had been lost, stolen or destroyed. In January 2000, several years after the shares represented by such certificates purportedly had been transferred, the original certificates were tendered to Merrill Lynch with instruction to sell the shares represented by such certificates. Merrill Lynch then sold such shares and tendered the certificates to AST for transfer, at which time AST confiscated the certificates. On March 28, 2000, the Company received a letter from counsel for Merrill Lynch. In that letter, Merrill Lynch advised the Company of its intention to enforce its clients' rights to compel the Company to recognize the transfers of the shares represented by the certificates tendered to it in January 2000 under the Uniform Commercial Code as adopted by the State of Utah. The Company complied with Merrill Lynch's demand. The net effect of this action was that the Company was required to recognize as having been previously issued 208,000 shares of common stock that were not then shown as being issued and outstanding on the books and records of the Company. On March 29, 2000, the Company filed a lawsuit in Utah state court against Mr. Wood, WAC Research, Inc. ("WAC") and Muito Bem Ltd Partnership ("Muito Bem"), Alpha Tech Stock Transfer & Trust Company, the Company's former stock transfer agent ("Alpha Tech"). Both WAC and Muito Bem are entities affiliated with Wood. The case sought damages from all defendants, and specifically asked the court to award to the Company the proceeds of the sales by WAC and/or Muito Bem of the shares that the Company was compelled to reinstate on the basis that those entities and their principals had been unjustly enriched. In a settlement, dated April 12, 2000, among Wood, WAC, Muito Bem, Merrill Lynch and the Company, the Company received cash in the amount of $200,714, in exchange for which it released its claims for further damages against Wood, WAC, Muito Bem and Merrill Lynch. The Company's claims against Alpha Tech are still pending.

On December 7, 1999, Donald M. Wood, the former Chairman and Chief Executive Officer of the Company, and the Stith Law Office (Wood's personal legal counsel) filed a lawsuit in the District Court of Salt Lake County, State of Utah (Case No. 990912153). In that lawsuit, Wood and Stith asserted that the Company has breached a Settlement Agreement executed by the Company and Wood upon Wood's resignation as the Company's Chairman and Chief Executive Officer, effective as of January 14, 1999. The lawsuit includes claims for breach of

contract, fraud and intentional infliction of emotional distress, and seeks money damages and punitive damages in the aggregate amount of $1,162,246. On February 7, 2000, the Company filed its answer to the Wood litigation, in which the Company asserted that its payment obligations under the Settlement Agreement were excused by repeated breaches by Wood of various covenants of the Settlement Agreement. Simultaneously, the Company filed a counterclaim against Wood for money damages incurred by the Company as a result of Wood's various breaches of the Settlement Agreement. The Company also simultaneously filed motions to dismiss the fraud and intentional infliction of emotional distress claims. The Company's management believes the Wood litigation is without merit and intends to vigorously defend.

On March 19, 1999, Alpha Tech Stock Transfer Company ("Alpha Tech") filed a lawsuit against the Company in Utah state court in Salt Lake City, Utah. Alpha Tech was the Company's stock transfer agent for a period of approximately ten years until the Company terminated its relationship with Alpha Tech in January 1999 and instructed Alpha Tech to transfer the Company's stock transfer records to American Stock Transfer, New York, New York. The complaint alleges that the Company breached its service contract with Alpha Tech by failing to pay $132,165 to Alpha Tech for transfer agent services rendered and reimbursement for legal expenses incurred by Alpha Tech. Alpha Tech never served the complaint; the Company learned about the complaint through an unrelated third party. In March 2000, Alpha Tech refiled essentially the same complaint, thereby commencing another lawsuit against the Company. The March 2000 complaint is virtually identical to the March 1999 complaint. In April 2000, the Company accepted service of process, and has filed a motion to dismiss the March 2000 complaint. The Company disputes the claims of Alpha Tech's complaint and intends to vigorously defend this action.

On April 27, 1998, the Enforcement Division of the Securities and Exchange Commission notified the Company that the SEC was anticipating filing an administrative proceeding in the latter part of calendar year 1998 against various individuals and entities who had engaged in transactions with a Canadian corporation. The SEC Enforcement Division further indicated that the Company may be named as a defendant in such administrative action. In July 1998, the Company submitted a Wells Submission to clarify why, in the Company's estimation, it should not be named in the administrative proceeding, if any. The Company suggested in the Wells Submission that it should not be named in any administrative proceeding because the Company never consummated either of the two transactions with the subject Canadian company that the Company was considering, and the Company received no consideration in connection with those aborted transactions. Moreover, the Company believes that its conduct in connection with those proposed but aborted transactions met applicable legal requirements. As of December 31, 2000, the Company had received no response from the Enforcement Division about whether the SEC plans to name the Company in any administrative action.

In addition, the Company has previously disclosed that, in the first quarter of 1999, it was informed of an investigation by the Enforcement Division of the Securities and Exchange Commission. The Company believes this investigation concerns certain trading activity in the Company's common stock and other transactions involving the Company's securities, however, the Company has not been informed of the specifics of such investigation. The Company has cooperated fully with these administrative proceedings. The Company had no contract from the Enforcement Division regarding this investigation during the entirety of 2000.

On February 12, 1998, Fuji Corporation filed a claim with the International Trade Commission seeking a cease and desist order against approximately 30 entities. Fuji sought to enlist the aid of the U.S. Customs

Department in preventing the importation of single-use cameras which are manufactured by any of the defendant entities and which infringe the patents of Fuji. The Company does not manufacture single-use cameras, but previously has distributed single-use cameras, which have been refurbished and reloaded in Mainland China. The Company was therefore involved in the Fuji proceeding. The Company engaged intellectual property counsel and vigorously defended its position until December 1998, when the Company sold its remaining inventory of single-use cameras to another entity. In connection with that sale, any liability of the Company in connection with the Fuji proceeding, including the costs of further defending the action, were assumed by the purchaser of the Company's single-use camera inventory, although the Company nominally remains part of that litigation.

The Company is involved in various other claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these other matters will not have a material adverse effect on the Company's operations or financial condition.

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

No.	Description
10.1	Convertible Debenture and Equity Line of Credit Agreement between the Company and five investors dated as of May 28, 1998. (Incorporated by reference from Current Report on Form 8-K filed by the Company with the SEC on June 8, 1998).
10.2	Form of Convertible Debentures issued in May 1998. (Incorporated by reference from Current Report on Form 8-K filed by the Company with the SEC on June 8, 1998).
10.3	Form of A Warrants issued in conjunction with Convertible Debentures. (Incorporated by reference from Current Report on Form 8-K filed by the Company with the SEC on June 8, 1998).
10.4	Form of B Warrants issued in conjunction with Convertible Debentures. (Incorporated by reference from Current Report on Form 8-K filed by the Company with the SEC on June 8, 1998).
10.5	Registration Rights Agreement entered into with the holders of Convertible Debentures. (Incorporated by reference from Current Report on Form 8-K filed by the Company with the SEC on June 8, 1998).
10.6	Modification Agreement between the Company and the holders of Convertible Debentures, dated as of June 25, 1999. (Incorporated by reference from Quarterly Report on Form 10-QSB for the period ended June 30, 1999).
10.7	Amendment to Modification Agreement between the Company and the holders of Convertible Debentures, dated as of November 12, 1999. (Incorporated by reference from Quarterly Report on Form 10-QSB for the period ended September 30, 1999.)

10.8 Convertible Debenture Retirement Agreement between the Company and the holders of the Convertible Debentures, dated as of February 1, 2000. (Incorporated by reference from Annual Report on Form 10-KSB for the year ended December 31, 1999.)

10.9 Stock Purchase Agreement between the Company and seven investors, dated as of February 11, 2000. (Incorporated by reference from Annual Report on Form 10-KSB for the year ended December 31, 1999.)

10.10 Employment Agreement between the Company and Frederick W. Volcansek, dated as of February 5, 1999. (Incorporated by reference from Annual Report on Form 10-KSB for the year ended December 31, 1998).

10.11 Employment Agreement between the Company and Lloyd M. Taggart, dated as of June 22, 1999. (Incorporated by reference from Quarterly Report on Form 10-QSB for the period ended September 30, 1999.)

10.12 Commercial Lease between the Company and FRE III Corporation, a California corporation, dated as of November 4, 1999. (Incorporated by reference from Quarterly Report on Form 10-QSB for the period ended September 30, 1999.)

10.13 Commercial Real Estate Purchase Contract between the Company and Darwin Datwyler dated as of July 16, 1999, as amended through November 4, 1999. (Incorporated by reference from Quarterly Report on Form 10-QSB for the period ended September 30, 1999.)

10.14 Stock Purchase Agreement between the Company and three investors, dated as of May 18, 2000. (Incorporated by reference from Quarterly Report on Form 10-QSB for the period ended June 30, 2000).

10.15 Asset Purchase Agreement dated November 22, 2000, by and among Dynatec International, Inc., and Expandable Home Organizers, Inc., a California corporation (Incorporated by reference from Current Report on Form 8-K dated as of November 22, 2000).

10.16 Form of Promissory Note in favor of Sarkat International, L.L.C. (Incorporated by reference from Annual Report on Form 10-KSB for the year ended December 31, 2000).

10.17 Articles of Organization of Nordic ASI, L.L.C. (Incorporated by reference from Annual Report on Form 10-KSB for the year ended December 31, 2000)

10.18 Operating Agreement of Nordic ASI, L.L.C. (Incorporated by reference from Annual Report on Form 10-KSB for the year ended December 31, 2000)

(b) Forms 8-K

None

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

DYNATEC INTERNATIONAL, INC.

/s/ Frederick W. Volcansek, Sr. May 14, 2001

Frederick W. Volcansek, Sr. Date
Chairman & CEO

/s/ Mark W. Sperry May 14, 2001

Mark W. Sperry Date
Vice President & Chief Accounting Officer

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