

PRO DEX INC
Form 10-Q
November 13, 2008
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2008

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 0-14942

PRO-DEX, INC.

UNITED STATES

(Exact name of Registrant as Specified in its Charter)

Colorado
(State or Other Jurisdiction of
Incorporation or Organization)

84-1261240
(IRS Employer Identification No.)

2361 McGaw Avenue, Irvine, California 92614

(Address of Principal Executive Offices)

Registrant's telephone number including area code: 949-769-3200

Indicate by check mark whether the registrant: (1) has filed all reports required by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes [X] No []

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer [] Accelerated Filer [] Non-Accelerated Filer [] Smaller reporting company [x]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes [] No [X]

Indicate the number of shares outstanding of each of the issuer's classes of common equity as of the latest practicable date: 9,702,288 shares of Common Stock, no par value, as of November 3, 2008.

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Pro-Dex, Inc.

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Item 1. Financial Statements**PRO-DEX, INC. and SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS**

| | <i>September 30, 2008</i> | <i>June 30, 2008</i> |
|--|---------------------------|----------------------|
| | <i>(unaudited)</i> | <i>(audited)</i> |
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 384,000 | \$ 517,000 |
| Accounts receivable, net of allowance for doubtful accounts of \$130,000 at September 30, 2008 and \$144,000 at June 30, 2008 | 3,183,000 | 2,842,000 |
| Other current receivables | - | 205,000 |
| Inventories | 4,640,000 | 5,101,000 |
| Prepaid expenses | 265,000 | 214,000 |
| Prepaid income taxes | 869,000 | 860,000 |
| Deferred income taxes | 1,182,000 | 1,176,000 |
| Total current assets | 10,523,000 | 10,915,000 |
| Property, plant, equipment, net | 6,416,000 | 6,470,000 |
| Other assets: | | |
| Goodwill | 2,997,000 | 2,997,000 |
| Intangibles - Patents, net | 1,197,000 | 1,221,000 |
| Other | 62,000 | 68,000 |
| Total other assets | 4,256,000 | 4,286,000 |
| Total assets | \$ 21,195,000 | \$ 21,671,000 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Credit Line | \$ 2,600,000 | \$ 2,000,000 |
| Accounts payable | 1,303,000 | 1,736,000 |
| Accrued expenses | 1,712,000 | 2,053,000 |
| Income taxes payable | - | 114,000 |
| Current portion of term note | 333,000 | 396,000 |
| Current portion of real estate loan | 31,000 | 30,000 |
| Total current liabilities | 5,979,000 | 6,329,000 |
| Long-term liabilities | | |
| Real estate loan | 1,553,000 | 1,560,000 |
| Patent deferred payable | 44,000 | 44,000 |
| Deferred income taxes | 290,000 | 290,000 |
| Deferred rent | 167,000 | 150,000 |

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| | | |
|---|---------------|---------------|
| Total long-term liabilities | 2,054,000 | 2,044,000 |
| Total liabilities | 8,033,000 | 8,373,000 |
| Commitments and contingencies | | |
| Shareholders' equity: | | |
| Common shares; no par value; 50,000,000 shares authorized; 9,738,437 shares issued and outstanding September 30, 2008, 9,803,366 shares issued and outstanding June 30, 2008, | 16,527,000 | 16,545,000 |
| Accumulated deficit | (3,365,000) | (3,247,000) |
| Total shareholders' equity | 13,162,000 | 13,298,000 |
| Total liabilities and shareholders' equity | \$ 21,195,000 | \$ 21,671,000 |

PRO-DEX, INC. and SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
Three months ended September 30 (unaudited)

| | 2008 | 2007 |
|---|--------------|--------------|
| Net sales | \$ 5,656,000 | \$ 5,992,000 |
| Cost of sales | 3,902,000 | 3,839,000 |
| Gross profit | 1,754,000 | 2,153,000 |
| Operating expenses: | | |
| Selling expenses | 344,000 | 323,000 |
| General and administrative expenses | 835,000 | 735,000 |
| Research and development costs | 731,000 | 575,000 |
| Total operating expenses | 1,910,000 | 1,633,000 |
| Income (loss) from operations | (156,000) | 520,000 |
| Other income (expense): | | |
| Other expense, net | - | 6,000 |
| Royalty income | 2,000 | 6,000 |
| Interest expense | (61,000) | (47,000) |
| Total | (59,000) | (35,000) |
| Income (loss) before provision (benefit) for income taxes | (215,000) | 485,000 |
| Provision (benefit) for income taxes | (97,000) | 159,000 |
| Net income (loss) | \$ (118,000) | \$ 326,000 |
| Net income (loss) per share: | | |
| Basic | \$ (0.01) | \$ 0.03 |
| Diluted | \$ (0.01) | \$ 0.03 |
| Weighted average shares outstanding - basic | 9,783,407 | 9,718,366 |
| Weighted average shares outstanding - diluted | 9,783,407 | 9,947,884 |

See notes to consolidated financial statements.

PRO-DEX, INC. and SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
Three months ended September 30 (unaudited)

| | 2008 | 2007 |
|---|--------------|------------|
| Cash Flows from Operating Activities: | | |
| Net Income (Loss) | \$ (118,000) | \$ 326,000 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 222,000 | 120,000 |
| Stock based compensation | 42,000 | 48,000 |
| (Recovery of) provision for doubtful accounts | (14,000) | (12,000) |
| Provision for slow moving and obsolete inventory | - | 15,000 |
| (Decrease) in deferred taxes | (5,000) | - |
| Changes in: | | |
| (Increase) decrease in accounts receivable | (122,000) | 481,000 |
| Decrease in inventories | 461,000 | 172,000 |
| (Increase) in prepaid expenses | (50,000) | (51,000) |
| (Increase) decrease in other assets | 5,000 | (12,000) |
| (Decrease) Increase in accounts payable and accrued expenses | (756,000) | 58,000 |
| (Decrease) in income taxes payable | (124,000) | (53,000) |
| Net Cash (used by) provided by Operating Activities | (459,000) | 1,092,000 |
| Cash Flows From Investing Activities: | | |
| Purchases of equipment and leasehold improvements | (144,000) | (344,000) |
| Net Cash used in Investing Activities | (144,000) | (344,000) |
| Cash Flows from Financing Activities: | | |
| Net borrowing (payments) on line of credit | 600,000 | (300,000) |
| Principal payments on term note | (63,000) | (63,000) |
| Principal payments on mortgage | (7,000) | (7,000) |
| Stock Repurchases | (60,000) | - |
| Net Cash provided by (used by) Financing Activities | 470,000 | (370,000) |
| Net Increase (decrease) in Cash and Cash Equivalents | (133,000) | 378,000 |
| Cash and Cash Equivalents, beginning of period | 517,000 | 403,000 |
| Cash and Cash Equivalents, end of period | \$ 384,000 | \$ 781,000 |
| <i>Supplemental Information</i> | | |
| Cash payments for interest | \$ 56,000 | \$ 45,000 |

| | | |
|--------------------------------|------|------------|
| Cash payments for income taxes | \$ - | \$ 215,000 |
|--------------------------------|------|------------|

See notes to consolidated financial statements.

PRO-DEX, INC. AND SUBSIDIARIES**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****NOTE 1. BASIS OF PRESENTATION**

The accompanying unaudited consolidated financial statements of Pro-Dex, Inc. (we , us , our , Pro-Dex or the Company) have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Regulation S-K. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. These financial statements should be read in conjunction with the audited financial statements presented in our Annual Report for the fiscal year ended June 30, 2008. In the opinion of management, all adjustments considered necessary for a fair presentation have been included. The results of operations for such interim periods are not necessarily indicative of the results that may be expected for the full year. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-KSB for the year ended June 30, 2008.

NOTE 2. INVENTORIES

Inventories are stated at the lower of cost (the first-in, first-out method) or market and consist of the following:

| | September 30, 2008 (unaudited) | June 30, 2008 (audited) |
|----------------------------------|-----------------------------------|----------------------------|
| Raw Materials | \$ 1,683,257 | \$ 1,874,302 |
| Work in process | 1,135,000 | 993,000 |
| Development costs under contract | 232,000 | 200,000 |
| Finished goods | 1,589,743 | 2,033,698 |
| Total inventories | \$ 4,640,000 | \$ 5,101,000 |

NOTE 3. WARRANTY

The warranty reserve is based on historical costs of warranty repairs and expected future identifiable warranty expenses. As of September 30, 2008, we carried a warranty reserve of \$878,000, which was comprised of \$60,000 for future warranty expenses related to products that are currently in the process of being repaired, \$776,000 for future warranty expenses related to products that are still in the field, and \$42,000 for our legacy dental and industrial products. Warranty expenses are reflected in the financial statements in cost of sales (COS). The total warranty expense reflected in the cost of sales was \$201,000 for the quarter ended September 30, 2008 and \$366,000 for the quarter ended September 30, 2007. The warranty accrual and expenses for the three months ended September 30, 2008 and 2007 are presented below:

| | Three months Ended September 30, | |
|----------------------------|----------------------------------|------------|
| | 2008 | 2007 |
| Beginning Balance | \$ 861,000 | \$ 469,000 |
| Cash cost reducing accrual | (184,000) | (392,000) |
| Increased reserve expensed | 201,000 | 366,000 |
| Ending Balance | \$ 878,000 | \$ 443,000 |

NOTE 4. NET INCOME PER SHARE

The following table reconciles the weighted average shares outstanding for basic and diluted net (loss) income per share for the periods indicated. For the period ending September 30, 2008, there were 61,332 potentially dilutive options not included as they would have been anti-dilutive due to the loss.

| | Three Months Ended September 30, | |
|---|----------------------------------|------------|
| | 2008 | 2007 |
| Net (loss) income | \$ (118,000) | \$ 326,000 |
| Basic net (loss) income per common share: | | |
| Weighted average number of common shares outstanding | 9,783,407 | 9,718,366 |
| Basic net (loss) income per common share | \$ (0.01) | \$ 0.03 |
| | | |
| Diluted net (loss) income per share: | | |
| Weighted average of common shares outstanding | 9,783,407 | 9,718,366 |
| Effect of potentially dilutive securities (options) | - | 195,355 |
| Effect of potentially dilutive securities (restricted shares) | - | 21,038 |
| Effect of potentially dilutive securities (warrants) | - | 13,125 |
| Weighted average number of common and shares - | | |
| Diluted | 9,783,407 | 9,947,884 |
| Diluted net (loss) income per common share | \$ (0.01) | \$ 0.03 |

NOTE 5. CREDIT FACILITIES

On November 1, 2007, our existing credit facility with Wells Fargo was replaced with an expanded facility with a total borrowing capacity of \$6,562,500. Included in the increase is an increase in the credit line borrowing availability

from \$2,000,000 to \$4,000,000. The credit line's terms require monthly interest payments at the prime rate of interest (5.00% at September 30, 2008); or LIBOR (4.0% at September 30, 2008) plus 1.75%, at our discretion, based on outstanding borrowings. The total effective interest rate at September 30, 2008 for borrowings on the credit line was 5.0%. The credit facility expires on November 1, 2009. In addition to the credit line, a term commitment is available for borrowings for amounts up to \$2,000,000. We can take advances against this commitment through November 1, 2008, at which time the outstanding borrowings against this commitment will be converted to a term loan, to be amortized and repaid over 60 months. The term commitment's terms require monthly interest payments at the prime rate of interest; or LIBOR plus 2.0%, at our discretion, based on outstanding borrowings. The borrowings from this term commitment were used for construction financing of tenant improvements for our Irvine, California facility. The term loan that was entered into in January 2006 to finance the Astromec purchase remains in place. As of September 30, 2008, there was a principal balance on this term loan of \$333,333 which is required to be fully paid-off in January 2010, in accordance with its amortization schedule. The term loan's terms require monthly interest payments at the prime rate of interest; or LIBOR plus 2.5%, at our discretion, based on outstanding borrowings, with no minimum interest charge. The total effective interest rate at September 30, 2008 for borrowings on the term loan was 5.0%. All assets of the Company except our Carson City land and building secure the outstanding borrowings from Wells Fargo. There was \$2,600,000 borrowed under the credit line and nothing borrowed against term commitment facility as of September 30, 2008. The total eligible additional borrowing capacity at September 30, 2008 was \$3,400,000. See Note 11 for additional information concerning the tenant improvement credit facility.

In March 2006, we entered into a 10-year mortgage with Union Bank of California for \$1,650,000. Its terms require monthly interest payments at a fixed rate of 6.73% based on outstanding borrowings. The principal payments on the mortgage note are based on a 25-year amortization of the note and are \$11,000 per month beginning May 1, 2006. The outstanding borrowings are secured by our Carson City land and building. There was an outstanding balance of approximately \$1,583,000 under the terms of this mortgage as of September 30, 2008.

There are certain financial and non-financial covenants that we must meet to be in compliance with the terms of the Wells Fargo credit facility (which includes the term loan and the line of credit), as amended, and the Union Bank mortgage. At September 30, 2008, we had a net loss which violated the quarterly loss covenant in the Wells Fargo credit facility. This covenant was waived by Wells Fargo at a charge of \$5,000. Consequently, we have included \$83,000 of debt related to the term note to short term debt from long term debt.

NOTE 7. INCOME TAXES

Deferred income taxes are provided on a liability method whereby deferred tax assets and liabilities are recognized for temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment. We have tax credit carry forwards totaling \$247,000 for state tax purposes that do not expire and can be carried forward indefinitely until fully utilized.

Significant management judgment is required in determining our provision for income taxes and the recoverability of our deferred tax asset. Such determination is based on our estimates of future taxable income by jurisdictions in which we operate and the period over which our deferred tax assets will be recoverable. In the event that actual results differ from these estimates or we adjust these estimates in future periods, we may need to establish a valuation allowance, which could result in a tax provision up to the carrying value of our deferred tax assets.

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As of September 30, 2008, we have accrued \$88,000 of uncertain tax positions related to various federal and state income tax matters. Of this total, \$79,000 relates to R&D credits and would reduce the Company's income tax expense if recognized and would result in a corresponding decrease in the Company's effective tax rate.

During the quarter, the Internal Revenue Service effectively settled its audit of our federal income tax returns for the fiscal years ended June 30, 2004 through June 30, 2006. This settlement resulted in the reversal of \$41,000 of unrecognized tax benefits associated with Section 263A costs we reported, which reduced our tax expense by \$6,000, thereby reducing our income tax benefit for the three months ended September 30, 2008. Our remaining FIN 48 tax liability as of September 30, 2008, related to the fiscal years ended June 30, 2004 through June 30, 2006, is \$88,000. We have not identified any new unrecognized tax benefits.

A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows:

| | |
|--|-------------|
| Balance at July 1, 2008 | \$114,000 |
| Additions based on tax positions related to the current year | 0 |
| Additions for tax positions of prior years | \$ 15,000 |
| Reductions for tax positions of prior years | 0 |
| Reduction for Settlements | (\$ 41,000) |
| | ----- |
| Balance at September 30, 2008 | \$ 88,000 |

We recognize accrued interest and penalties related to unrecognized tax benefits in income tax expense. As of September 30, 2008, we had approximately \$26,000 in accrued interest and penalties which is included as a component of the \$88,000 unrecognized tax benefit noted above. The liability for the payment of interest and penalties has increased by approximately \$15,000 for the three months ended September 30, 2008.

Pro-Dex and its subsidiary are subject to U.S. federal income tax, as well as income tax of multiple state tax jurisdictions. We are currently open to audit under the statute of limitations by the Internal Revenue Service for the years ended June 30, 2007 through June 30, 2008. The Company's state income tax returns are open to audit under the statute of limitations for the years ended June 30, 2004 through June 30, 2008. The company does not anticipate a significant change to the total amount of unrecognized tax benefits within the next 12 months.

NOTE 8. SHARE-BASED COMPENSATION

Share-based compensation expense recognized under SFAS 123(R) for the three months ended September 30, 2008 and 2007 was \$42,000 and \$48,000, respectively, which was related to stock options and restricted stock grants vesting in 2008 and 2007. Share-based compensation expense reduced our results of operations as follows:

| | Three months ended September 30, (unaudited) | |
|--|---|-----------|
| | 2008 | 2007 |
| Share-based compensation expense recognized: | | |
| General and administrative, options | \$ 13,000 | \$ 19,000 |
| General and administrative, restricted stock | 29,000 | 29,000 |
| Subtotal expense | 42,000 | 48,000 |
| Related deferred tax benefit | (12,000) | (12,000) |
| Decrease in net income | \$ 30,000 | \$ 36,000 |
| | | |
| Decrease in basic earnings per share | \$ 0.00 | \$ 0.00 |
| Decrease in diluted earnings per share | \$ 0.00 | \$ 0.00 |

As of September 30, 2008, there was \$98,736 of total unrecognized compensation cost related to 146,750 non-vested outstanding stock options with a per share weighted average price of \$1.46. The unrecognized expense is anticipated to be recognized on a straight-line basis over a weighted average period of 1.0 years. The following is a summary of stock option activity in the three months ending September 30:

| | 2008 | Weighted- | 2007 | Weighted- |
|---|-----------|---------------------------|-----------|---------------------------|
| | Shares | Average Exercise Price | Shares | Average Exercise Price |
| Fixed Options | | | | |
| Outstanding at beginning of fiscal year (7/1) | 1,109,500 | \$ 1.58 | 1,038,500 | \$ 1.60 |
| Granted | 30,000 | 0.96 | 30,000 | 1.55 |
| Exercised | - | - | - | - |
| Forfeited | - | - | - | - |
| Outstanding at end of period (9/30) | 1,139,500 | \$ 1.58 | 1,068,500 | \$ 1.60 |
| Exercisable at end of period (9/30) | 992,750 | \$ 1.60 | 881,250 | \$ 1.56 |
| Weighted-average fair value per Option granted during the period | | \$ 0.45 | | \$ 0.81 |

The following table summarizes information regarding options outstanding and options exercisable at September 30, 2008:

| Range of Exercise Price | Number Outstanding | Options Outstanding | | | Options Exercisable | | |
|-------------------------|--------------------|---|---------------------------------|---------------------------|---------------------------------|---------------------------|------------------|
| | | Weighted-Average Remaining Contractual Life | Weighted-Average Exercise Price | Aggregate Intrinsic Value | Weighted-Average Exercise Price | Aggregate Intrinsic Value | |
| \$0.42 to \$0.81 | 260,000 | 3.5 years | \$ 0.70 | \$ 65,400 | 260,000 | \$ 0.70 | \$ 65,400 |
| \$1.08 to \$1.56 | 462,000 | 6.4 years | 1.32 | \$ 450 | 327,750 | 1.38 | \$ - |
| \$1.74 to \$2.18 | 242,500 | 3.5 years | 2.04 | \$ - | 242,500 | 2.04 | \$ - |
| \$2.44 to \$3.30 | 175,000 | 6.8 years | 2.77 | \$ - | 162,500 | 2.79 | \$ - |
| Total | 1,139,500 | 5.2 years | \$ 1.58 | \$ 65,850 | 992,750 | \$ 1.60 | \$ 65,400 |

Restricted Stock

The following is a summary of restricted share activity in the three months ending September 30:

| | 2008 | | 2007 | |
|---|---------|---------------------------------|---------|---------------------------------|
| | Shares | Weighted-Average Exercise Price | Shares | Weighted-Average Exercise Price |
| Restricted shares Outstanding at beginning of fiscal year (7/1) | 170,000 | \$ 1.38 | 255,000 | \$ 1.38 |
| Granted | - | - | - | - |
| Issued | - | \$ - | - | - |
| Forfeited | - | - | - | - |
| Outstanding at end of period (9/30) | 170,000 | \$ 1.38 | 255,000 | \$ 1.38 |

| | | | | |
|-------------------------------------|---------|---------|---|------|
| Exercisable at end of period (9/30) | 120,417 | \$ 1.38 | - | \$ - |
|-------------------------------------|---------|---------|---|------|

As of September 30, 2008, there was \$166,175 of total unrecognized compensation cost related to 120,417 non-vested outstanding restricted shares with a per share weighted average price of \$1.38. The unrecognized expense is anticipated to be recognized on a straight-line basis over a period of 1.4 years.

Stock Warrants

At September 30, 2008, warrants to acquire 100,000 shares of common stock were outstanding. These warrants are fully vested, have a weighted-average exercise price of \$1.25 and a weighted-average remaining life of 0.75 years.

NOTE 9. MAJOR CUSTOMERS

We had two major customers (defined as a customer that represents greater than 10% of the Company's total revenues) in the three months ended September 30, 2008 and 2007.

| | Three months ended September 30, (unaudited) | | | |
|------------|---|-------------|--------------|-------------|
| | 2008 | | 2007 | |
| | Revenues | Accts. Rec. | Revenues | Accts. Rec. |
| Customer 1 | \$ 1,046,000 | \$ 409,000 | \$ 1,319,000 | \$ 431,000 |
| Customer 2 | \$ 1,408,000 | \$ 978,000 | \$ 1,235,000 | \$ 563,000 |

NOTE 10. COMMITMENTS AND CONTINGENCIES

Our manufacture and distribution of certain products involves a risk of legal action, and, from time to time, we are named as defendants in lawsuits. It is not reasonably possible to estimate the awards or damages, or the range of awards or damages, if any, we might incur in connection with such litigation. Other than the case pending with the Orange County Water District, management is not aware of any material actual, pending or threatened litigation at this time.

On June 23, 2008, the Orange County Water District (OCWD) filed a complaint in the Superior Court of the State of California in the County of Orange concerning remediation of alleged ground water contamination in the Orange County Groundwater South Basin; Orange County Water District v. Sabic Innovative Plastics U.S. LLC, et al., Case No. 00078246. The South Basin underlies parts of Santa Ana, California and adjacent cities. The complaint identifies 17 named defendants, including Pro-Dex, and also designates 400 unnamed Doe defendants. .. The Company moved out of this Santa Ana site in April, 2008 and has no remaining operations there.

The complaint alleges that the defendants contaminated the South Basin with volatile organic chemicals (VOCs) and perchlorate through various activities at properties each defendant now controls or has controlled in the past. Through its lawsuit, the OCWD seeks compensatory relief for all its own remedial activities, and injunctive relief to compel the defendants to undertake remedial activities in general. The complaint does not, however, specify any remedial activities that the OCWD has undertaken to date or any remedial activities that it seeks any particular defendants to undertake. Moreover, from our investigation of OCWD s remedial activities to date, we have determined that the OCWD is in the early stages of its remedial investigation for the South Basin groundwater contamination.

As noted above, 16 other entities are named defendants in this case along with Pro-Dex. While some are small businesses, others are larger corporations or their subsidiaries. Further, as this case progresses, the OCWD is likely to add at least a few more named defendants to the case from the 400 Doe defendants it has designated in the current complaint. In the indeterminable event that Pro-Dex would be held liable in the case, OCWD s total recovery probably would be allocated among several defendants, each of which would pay only a proportionate share of that total recovery.

Because of the vagueness of the complaint, the early stage of the OCWD s remedial activities in the South Basin, and the likelihood that any recovery the OCWD may gain will be allocated among several defendants, our liability, as well as our costs of defending, monitoring and concluding our involvement in this case are uncertain, and those costs

cannot now be estimated.

NOTE 11. SUBSEQUENT EVENT

On October 1, 2008, we converted the full \$2,000,000 available under the term commitment portion of the credit facility from the open credit facility to the term commitment. This facility is expected to be converted to a five year term loan in November 2008, and amortized and repaid over 60 months. Its initial terms were to require monthly interest payments at the prime rate of interest (5.0% at September 30, 2008); or LIBOR (4.0% at September 30, 2008) plus 2.0%, at our discretion, based on outstanding borrowings, but now are expected to be effectively fixed at a rate of approximately 5.9%. As of November 11, 2008, the conversion to a five-year loan has not taken place and the amount borrowed remains as a short term credit line with the interest rates at the prime rate of interest; or LIBOR plus 2.0%, at our discretion.

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

COMPANY OVERVIEW

The following discussion and analysis provides information that the Company's management believes is relevant to an assessment and understanding of our results of operations and financial condition for each of the three month periods ended September 30, 2008 and 2007. This discussion should be read in conjunction with the Consolidated Financial Statements and the Notes thereto included elsewhere in this Report. This Report contains certain forward-looking statements and information. The cautionary statements included herein should be read as being applicable to all related forward-looking statements wherever they may appear. Our actual future results could differ materially from those discussed herein. Our critical accounting policies relate to inventory valuation for slow moving items, impairment of goodwill, warranty reserves, and recoverability of deferred income taxes.

Except for the historical information contained herein, the matters discussed in this Quarterly Report on Form 10-Q, including discussions of our product development plans, business strategies and market factors influencing our results, are forward-looking statements that involve certain risks and uncertainties. Actual results may differ from those anticipated by us as a result of various factors, both foreseen and unforeseen, including, but not limited to, our ability to continue to develop new products and increase systems sales in markets characterized by rapid technological evolution, consolidation within our target marketplace and among our competitors, and competition from larger, better capitalized competitors. Many other economic, competitive, governmental and technological factors could impact our ability to achieve our goals. Interested persons are urged to review the risks described herein, as well as in our other public disclosures and filings with the Securities and Exchange Commission. We refer you to the risk factors and cautionary language contained in our reports filed with the Securities and Exchange Commission from time to time, including, but not limited to, those risks and uncertainties which may be listed in our Annual Report on Form 10-K or 10-KSB.

Pro-Dex, Inc. (Company, Pro-Dex , we, our, , us), with operations in Irvine, California, Beaverton, Oregon and City, Nevada, provides a pathway to product solutions never envisioned by customers. A unique blend of creativity and systemic discipline enables us to develop and manufacture innovative designs that powerfully complete a customer s strategic product offering. Pro-Dex leverages extraordinary human collaboration and superior technical capability to power and control products used in medical, aerospace, military, research and industrial applications requiring high precision in harsh environments. With expertise in multi-axis motion control, fractional horsepower motors and rotary drive systems, we identify and create unexpected value for our customers.

Pro-Dex's products are found in hospitals, dental offices, medical engineering labs, commercial and military aircraft, scientific research facilities and high tech manufacturing operations around the world. The names of Micro Motors, Oregon Micro Systems, and Astromec are used for marketing purposes as brand names.

Pro-Dex's principal headquarters changed April 28, 2008 and we are located at 2361 McGaw Avenue, Irvine, California 92614 and our phone number also changed to 949-769-3200. Our Internet address is www.pro-dex.com. Our annual reports on Form 10-KSB, quarterly reports on Form 10-Q, current reports on Form 8-K, amendments to those reports and other SEC filings, are available free of charge through our website as soon as reasonably practicable after such reports are electronically filed with, or furnished to, the SEC. In addition, our Code of Ethics and other corporate governance documents may be found on our website at the Internet address set forth above. Our filings with the SEC may also be read and copied at the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. You may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC at www.sec.gov.

Description of Business

The majority of our revenue is derived from designing, developing and manufacturing rotary drive systems for the medical device and dental industries, motion control software and hardware for industrial and scientific applications and fractional horsepower DC motors for aerospace, medical and military applications. A large part of the revenue of the Company has been driven by developing and selling numerous types of private label rotary drive systems for use in dental procedures, as well as cranial, spinal, arthroscopic and orthopedic surgery. The Company distributes its own line of pneumatic and electric dental hand pieces sold under the Micro Motors name utilizing a network of independent sales representatives across North America. Other revenue sources include designing and manufacturing miniature pneumatic motors, fractional horsepower DC motors and motion control systems for industrial applications in the automotive, aerospace, and apparel industries.

Company-funded research and development supports the development of generic rotary drive, motion control, and electric motor technology platforms. Company-funded research and development projects are generally expected to convert to customer-funded projects within six to eighteen months. Company funded project costs not associated with signed contracts or purchase orders are expensed as incurred.

In the three months ended September 30, 2008, \$731,000 was expensed for company-funded research and development; an increase of \$156,000 from the \$575,000 expensed in the three months ended September 30, 2007. The increase was attributable to increased labor costs for medical and small motor product development, improvement and validation.

We seek customer-funded projects to customize these platforms to specific customer requirements. For customer-funded development projects, costs are capitalized and recognized as a cost of sales when specific deliverables within the development contracts are earned, matching the costs to the revenue.

| Customer-funded development (\$'000) | Three Months Ended September 30, | |
|---|----------------------------------|-------|
| | 2008 | 2007 |
| Revenue | \$ 132 | \$ 92 |
| Cost of Sales | 57 | 31 |

| | | | | | | |
|--------------|----|----|-----|----|----|-----|
| Gross margin | \$ | 75 | 57% | \$ | 61 | 66% |
|--------------|----|----|-----|----|----|-----|

Customer-funded research and development fees increased in the quarter ended September 30, 2008 due to work being completed on projects signed in the preceding 12 months. The results of customer-funded development work are intended to provide long-term exclusive manufacturing agreements and may provide the customer with the retention of the intellectual property developed. The identity of our customers is generally protected by a non-disclosure agreement.

The Company's revenue is derived from five main customer types. The proportion of total sales to each customer type and sales by location are noted in the tables below (unaudited):

| Sales by customer type (\$'000) | Three months Ended September 30, | | | |
|---------------------------------|----------------------------------|------|----------|------|
| | 2008 | | 2007 | |
| Dental | \$ 731 | 13% | \$ 963 | 16% |
| Medical | 2,676 | 47% | 2,918 | 49% |
| Industrial | 944 | 17% | 1,001 | 17% |
| Aerospace | 765 | 14% | 563 | 9% |
| Government, repairs and other | 540 | 10% | 547 | 9% |
| Total Sales | \$ 5,656 | 100% | \$ 5,992 | 100% |

Medical product sales represent the manufacture of products that utilize proprietary designs developed by us under exclusive design and supply agreements. Our dental products are primarily sold to original equipment manufacturers and dental product distributors. An independent dealer network markets our own branded line of dental products; including the Intraflow™ dental anesthesia product. We also design and manufacture embedded multi-axis motion controllers used to regulate the motion of servo and stepper motors, predominantly for the factory automation, scientific research, and medical analysis equipment industries. The controllers support the platforms for PCI, VME, ISA, and cPCI busses as well as stand-alone requirements. In addition, we make and sell pneumatic motors for industrial applications that are marketed directly to end-users and through industrial supply distributors. The Carson City products include high reliability fractional horsepower DC motors designed for harsh environments, primarily for the aerospace and medical markets.

We hold the following three independently verified certifications: ISO 9001:2000, ISO 13485 revised 1998, and Medical Device Directive 93/42/EEC Annex II company.

At the present time, we are generally able to fill orders within sixty (60) days. At September 30, 2008, we had a backlog, including orders for delivery beyond 60 days, of \$8.0 million compared with a backlog of \$9.4 million at September 30, 2007 and \$10.4 million at June 30, 2008. We expect to ship most of our backlog in fiscal year 2009 and the remainder in fiscal year 2010. The decreased backlog compared to September 2007 and June 2008 is due to normal fluctuations in the timing of receipt and shipment of orders. We do not typically experience seasonal fluctuations in our new order bookings, but may experience variability in our new order bookings due to the timing of major new product launches. Similarly, we do not typically experience seasonal fluctuations in our shipments and revenues.

RESULTS OF OPERATIONS**For the Three-Month periods ended September 30, 2008 and 2007**

The following table sets forth the periods indicated and the percentage of net revenues represented by each item in our Consolidated Statements of Operations.

| (In Thousands) | Three Months Ended September 30, | | | |
|--|----------------------------------|------|----------|------|
| | 2008 | | 2007 | |
| Net sales: | \$ 5,656 | 100% | \$ 5,992 | 100% |
| Cost of sales | 3,902 | 69% | 3,839 | 64% |
| Gross Profit | 1,754 | 31% | 2,153 | 36% |
| Selling, general and administrative expenses | 1,179 | 21% | 1,058 | 18% |
| Research and development costs | 731 | 13% | 575 | 10% |
| Income from Operations | (156) | -3% | 520 | 9% |
| Net interest and other expense | 59 | 1% | 35 | 1% |
| Earnings before provision for income taxes | (215) | -4% | 485 | 8% |
| Provision for income taxes | (97) | -2% | 159 | 3% |
| Net income | \$ (118) | -2% | \$ 326 | 5% |

Net Sales. Consolidated sales decreased from \$5,992,000 to \$5,656,000 (\$336,000 or 6%) for the quarter ended September 30, 2008 compared to the quarter ended September 30, 2007. The decrease was due to a reduced volume of a single medical customer, offsetting increases in revenues to the aerospace customers.

Although selective price increases and decreases were implemented in response to market conditions, the majority of the sales changes for each product line are due primarily to changes in sales volume, not the effect of price changes.

Gross Profit and Gross Profit Percentage of Sales. Our consolidated gross profit for the quarter ended September 30, 2008 decreased \$399,000 or 19% over the same quarter in the previous year due to the lower level of sales and a less favorable sales mix. Gross profit as a percentage of sales decreased to 31% for the quarter ended September 30, 2008 compared to 36% for the quarter ended September 30, 2007. Gross profit margins were reduced approximately 5 margin points also due to a less favorable sales mix. Gross profit and gross profit as a percentage of sales were as follows:

| | Three Months Ended September 30, | | |
|----------------------------------|----------------------------------|--------------|----------|
| | 2008 | 2007 | Decrease |
| Gross Profit | \$ 1,754,000 | \$ 2,153,000 | -19% |
| Gross Profit Percentage of Sales | 31% | 36% | |

Selling, General and Administrative Costs (S, G&A). Consolidated S, G & A expenses increased to \$1,180,000 for the quarter ended September 30, 2008 from \$1,058,000 for the quarter ended September 30, 2007. The increase in selling expense is mainly due to higher labor and labor related costs (\$14,000) and higher advertising costs (\$10,000). The increase in G & A costs was due to higher labor costs (\$50,000) and costs associated with Sarbanes Oxley compliance (\$61,000). As a percentage of sales, S, G&A expenses increased to 21% of sales from 18% of sales for the quarters ended September 30, 2008 and 2007, respectively. S, G&A costs were as follows:

| | Three Months Ended September 30, | | |
|----------------------------|----------------------------------|--------------|----------|
| | 2008 | 2007 | Increase |
| Selling | \$ 344,000 | \$ 323,000 | 7% |
| General and administrative | \$ 836,000 | \$ 735,000 | 14% |
| Total S, G&A | \$ 1,180,000 | \$ 1,058,000 | 12% |
| S, G&A Percentage of Sales | 21% | 18% | |

Research and Development (R&D) Costs. Company-funded research and development expenses increased \$156,000 to \$731,000 for the quarter ended September 30, 2008 from \$575,000 for the quarter ended September 30, 2007, an increase of 27%. The increase was due to approximately \$125,000 in higher labor and related costs and \$22,000 in independent research project costs associated with engineers working on company-funded projects. As a percentage of sales, company-funded research & development expenses increased to 13% of sales from 10% of sales for the quarters ended September 30, 2008 and 2007, respectively. Company-funded research and development costs were as follows:

| | Three Months Ended September 30, | | |
|--------------------------------|----------------------------------|------------|----------|
| | 2008 | 2007 | Increase |
| Research and Development costs | \$ 731,000 | \$ 575,000 | 27% |
| R & D Percentage of Sales | 13% | 10% | |

Operating Profit (loss) and Operating Profit (loss) Percentage of Sales. Our consolidated operating loss for the quarter ended September 30, 2008 was (\$156,000) compared to an operating profit of \$520,000 for the same quarter in the previous year. The decrease in operating profit was due to a lower gross profit caused by lower sales as previously described,, higher R&D costs and higher S,G&A. Consequently, operating loss as a percentage of sales was -3% for

the quarter ended September 30, 2008 compared to a 9% profit for the quarter ended September 30, 2007. Operating profit and margin were as follows:

| | Three Months Ended September 30, Increase | | |
|--------------------------------------|---|------------|------------|
| | 2008 | 2007 | (Decrease) |
| Operating Profit | \$ (156,000) | \$ 520,000 | -130% |
| Operating Profit Percentage of Sales | -3% | 9% | |

Royalties and Other Income. We received \$1,600 in royalty income in the three months ended September 30, 2008 compared to \$5,800 in the same period during the prior year.

Net Interest Expense. Net interest expense for the quarter ended September 30, 2008 was \$61,000 compared to \$43,000 in the quarter ended September, 2007, due to the higher debt levels through the quarter ended September 30, 2008.

Income Tax (Benefit) Provision. Our estimated effective combined federal and state tax rate on income from operations for the quarter ended September 30, 2008 resulted in a 45% credit of earnings before tax compared to a 33% provision of earnings before tax for the quarter ended September 30, 2007. The 2008 rate is reduced by a recalculation of the FIN 48 estimated tax and interest liability and the 2007 rate is reduced due to the use of estimated R&D state tax credits.

Net (Loss) Income. Our net (loss) income for the three months ended September 30, 2008 was (\$118,000) or (\$0.01) per share on a basic and diluted basis, as compared to a net income of \$326,000 or \$0.03 per share on a basic and diluted basis for the three months ended September 30, 2007.

Liquidity and Capital Resources

The following table presents selected financial information as of the end of quarters ended September 30, 2008 and 2007 as well as of the year ended June 30, 2008:

| | As of September 30, | | As of |
|---|---------------------|--------------|---------------|
| | 2008 | 2007 | June 30, 2008 |
| Cash and cash equivalents | \$ 384,000 | \$ 781,000 | \$ 517,000 |
| Working Capital ¹ | \$ 4,544,000 | \$ 6,621,000 | \$ 4,586,000 |
| Credit Line outstanding balance | \$ 2,600,000 | \$ 0 | \$ 2,000,000 |
| Tangible book value/common share ² | \$ 0.92 | \$ 0.91 | \$ 0.93 |
| Number of days of sales outstanding (DSO) in accounts receivable at end of quarter ³ | 51 | 45 | 48 |

¹ Working Capital = Ending Current Assets less Ending Current Liabilities.

² Tangible book value/common share = (Total shareholders equity - Net intangible asset (patents) - Goodwill) / (basic outstanding shares).

³ DSO = Ending Net Accounts Receivable balance / (Previous Quarter Sales / 91).

Our working capital at September 30, 2008 decreased to \$4.5 million compared to \$6.6 million at September 30, 2007 and \$4.6 million at June 30, 2008. Cash flow used by operations was \$458,000 in the three months ended September 30, 2008 compared to a cash flow provided by operations of \$1,092,000 for the three months ended September 30, 2007. The decrease in working capital and reduction in operating cash flow was due to an increase in A/R, a reduction in payables and accrued expenses within our normal payment processing cycle.

On November 1, 2007, our existing credit facility with Wells Fargo was replaced with an expanded facility with a total borrowing capacity of \$6,562,500. Included in the increase is an increase in the credit line borrowing availability from \$2,000,000 to \$4,000,000. The credit line's terms require monthly interest payments at the prime rate of interest (5.00% at September 30, 2008); or LIBOR (4.0% at September 30, 2008) plus 1.75%, at our discretion, based on outstanding borrowings. The total effective interest rate at September 30, 2008 for borrowings on the credit line was 5.0%. The credit facility expires on November 1, 2009. In addition to the credit line, a term commitment is available for borrowings for amounts up to \$2,000,000. We can take advances against this commitment through November 1, 2008, at which time the outstanding borrowings against this commitment will be converted to a term loan, to be amortized and repaid over 60 months. The term commitment's terms require monthly interest payments at the prime rate of interest; or LIBOR plus 2.0%, at our discretion, based on outstanding borrowings. The borrowings from this term commitment were used for construction financing of tenant improvements for our Irvine, California facility. The term loan that was entered into in January 2006 to finance the Astromec purchase remains in place. As of September 30, 2008, there was a principal balance on this term loan of \$333,333 which is required to be fully paid-off in January 2010, in accordance with its amortization schedule. The term loan's terms require monthly interest payments at the prime rate of interest; or LIBOR plus 2.5%, at our discretion, based on outstanding borrowings, with no minimum interest charge. The total effective interest rate at September 30, 2008 for borrowings on the term loan was 5.0%. All assets of the Company except our Carson City land and building secure the outstanding borrowings from Wells Fargo. There was \$2,600,000 borrowed under the credit line and nothing borrowed against term commitment facility as of September 30, 2008. The total eligible additional borrowing capacity at September 30, 2008 was \$3,400,000.

At September 30, 2008, we had cash and cash equivalents of \$384,000. We believe that our cash and cash equivalents on hand, together with cash flows from operations, if any, and amounts available under the credit facilities will be sufficient to meet our working capital and capital expenditure requirements for this and the next year.

In September 2002, our Board of Directors authorized the repurchase on the open market of up to 500,000 shares of our outstanding Common Stock at a share price no greater than \$1.25, subject to compliance with applicable laws and regulations. There is no requirement that we repurchase all or any portion of such shares. The maximum total value of the repurchase is not to exceed \$500,000. From the inception of the repurchase authorization through the fiscal year-end date of June 30, 2003, we repurchased 75,700 shares of Common Stock for \$43,741, at an average price of \$0.58 per share. No additional shares were repurchased in fiscal years 2004 through 2008. We started repurchasing shares again in the first quarter of fiscal year 2009. During the quarter, we repurchased 64,929 shares of common stock for \$58,924, at an average price of \$.91 per share. Since the initiation of the buyback in 2002 through September 30, 2008, we have repurchased 140,299 shares for \$102,665 at an average price of \$0.73 per share.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Not applicable.

Item 4. Controls and Procedures

The Chief Executive Officer and Chief Financial Officer (the principal executive officer and principal financial officer, respectively) conducted an evaluation of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (Exchange

Act)). Based on that evaluation for the quarter ended September 30, 2008, the Chief Executive Officer and Chief Financial Officer concluded that the disclosure controls and procedures are effective to ensure that information required to be disclosed by use in the reports filed or submitted by us under the Exchange Act is accumulated, recorded, processed, summarized and reported to management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, and to allow timely decisions regarding whether or not disclosure is required.

During the quarter ended September 30, 2008, there were no changes in our internal controls over financial reporting (as defined in Rule 13a-15(f) and 15d-15(f) under the Exchange Act) that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

PART II

OTHER INFORMATION

Item 1. Legal Proceedings

On June 23, 2008, the Orange County Water District (OCWD) filed a complaint in the Superior Court of the State of California in the County of Orange concerning remediation of alleged ground water contamination in the Orange County Groundwater South Basin; Orange County Water District v. Sabic Innovative Plastics U.S. LLC, et al., Case No. 00078246. The South Basin underlies parts of Santa Ana, California and adjacent cities. The complaint identifies 17 named defendants, including Pro-Dex, and also designates 400 unnamed Doe defendants. The Company moved out of this Santa Ana site in April, 2008 and has no remaining operations there.

The complaint alleges that the defendants contaminated the South Basin with volatile organic chemicals (VOCs) and perchlorate through various activities at properties each defendant now controls or has controlled in the past. Through its lawsuit, the OCWD seeks compensatory relief for all its own remedial activities, and injunctive relief to compel the defendants to undertake remedial activities in general. The complaint does not, however, specify any remedial activities that the OCWD has undertaken to date or any remedial activities that it seeks any particular defendants to undertake. Moreover, from our investigation of OCWD 's remedial activities to date, we have determined that the OCWD is in the early stages of its remedial investigation for the South Basin groundwater contamination.

As noted above, 16 other entities are named defendants in this case along with Pro-Dex. While some are small businesses, others are larger corporations or their subsidiaries. Further, as this case progresses, the OCWD is likely to add at least a few more named defendants to the case from the 400 Doe defendants it has designated in the current complaint. In the indeterminable event that Pro-Dex would be held liable in the case, OCWD 's total recovery probably would be allocated among several defendants, each of which would pay only a proportionate share of that total recovery.

Because of the vagueness of the complaint, the early stage of the OCWD 's remedial activities in the South Basin, and the likelihood that any recovery the OCWD may gain will be allocated among several defendants, our liability, as well as our costs of defending, monitoring and concluding our involvement in this case are uncertain, and those costs cannot now be estimated.

In general, we are from time to time a party to various legal proceedings incidental to our business, other than the above, none of which we consider may be material at this time. There can be no certainty that we may not ultimately incur liability or that such liability will not be material and adverse.

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

ISSUER PURCHASES OF SECURITIES

The table below sets forth information with respect to purchases of the Company's common stock made by or on behalf of the Company during the quarter ended September 30, 2008.

| Period | (a) Total Number of Shares Purchased | (b) Average Price Paid Per Share | (c) Total Number of Shares Purchased as Party of Publicly Announced Plans or Programs | (d) Maximum Number (or Approximate Dollar Value) of Shares that May Yet be Purchased Under the Plans or Programs |
|----------------------|---|---|--|---|
| July 1-31, 2008 | 15,700 | \$0.99 | 91,400 | 408,600 (\$440,719) |
| August 1-31, 2008 | 7,000 | \$0.94 | 98,400 | 401,600 (\$434,109) |
| September 1-30, 2008 | 42,229 | \$0.87 | 140,629 | 359,371 (\$397,335) |
| Total | 64,929 | \$0.91 | 140,629 | 359,371 (\$397,335) |

In September 2002, our Board of Directors authorized the repurchase on the open market of up to 500,000 shares of our outstanding Common Stock at a share price no greater than \$1.25, subject to compliance with applicable laws and regulations. There is no requirement that we repurchase all or any portion of such shares. The maximum total value of the repurchase is not to exceed \$500,000. This repurchase is to be financed with cash generated by operations. From the inception of the repurchase authorization through the fiscal year-end date of June 30, 2003, we repurchased 75,700 shares of Common Stock for \$43,741, at an average price of \$0.58 per share. No additional shares were repurchased in fiscal years 2004 through 2008. We started repurchasing shares again in the first quarter of fiscal year 2009. During the quarter, we repurchased 64,929 shares of common stock for \$58,924, at an average price of \$0.91 per share. Since the initiation of the buyback in 2002 through September 30, 2008, we have repurchased 140,629 shares for \$102,665 at an average price of \$0.73 per share.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. Submissions of Matters to a Vote of Securities Holders.

None.

Item 5. Other Information

Delisting Notice

On September 23, 2008, the Company received a letter from The Nasdaq Stock Market (Nasdaq) indicating that the bid price of its common stock for the last 30 consecutive business days had closed below the minimum \$1.00 per share required for continued listing under Nasdaq Marketplace Rule 4310(c)(4). Pursuant to Nasdaq Marketplace Rule 4310(c)(8)(D), the Company has been provided an initial period of 180 calendar days to regain compliance. The letter provided for the compliance dates of until March 23, 2009. The letter states the Nasdaq staff will provide written notification that the Company has achieved compliance with Rule 4310(c)(4) if at any time before March 23, 2009, the bid price of the Company's common stock closes at \$1.00 per share or more for a minimum of 10 consecutive business days, although the letter also states that the Nasdaq staff has the discretion to require compliance for a period in excess of 10 consecutive business days, but generally no more than 20 consecutive business days, under certain circumstances. On October 22, 2008, we received a letter from Nasdaq that extended our compliance deadline from March 23, 2009 to June 26, 2009.

If the Company cannot demonstrate compliance with Rule 4310(c)(4) by June 26, 2009, the Nasdaq staff will determine whether the Company meets The Nasdaq Capital Market initial listing criteria set forth in Nasdaq Marketplace Rule 4310(c), except for the bid price requirement. If the Company meets the initial listing criteria, the Nasdaq staff will notify the Company that it has been granted an additional 180 calendar day compliance period. If the Company is not eligible for an additional compliance period, the Nasdaq staff will provide written notice that the Company's securities will be delisted. At that time, the Company may appeal the Nasdaq staff's determination to delist its securities to a Listing Qualifications Panel.

If our common stock is delisted from the Nasdaq Capital Market, we could seek to have our common stock listed on other Nasdaq markets. However, delisting of our common stock from the Nasdaq Capital Market could hinder your ability to sell, or obtain an accurate quotation for the price of, your shares of our common stock. Delisting could also adversely affect the perception among investors of Pro-Dex and its prospects, which could lead to further declines in the market price of our common stock. Delisting would also make it more difficult and expensive for us to raise capital. In addition, delisting might subject us to an Securities and Exchange Commission rule that could adversely affect the ability of broker-dealers to sell or make a market in our common stock, thus hindering your ability to sell your shares.

Executive Compensation

Mr. Murphy has notified the Company that he is voluntarily waiving the current annual CPI adjustment to his base salary for 2008 (an amount equal to approximately \$1,220 per month), from November 1, 2008 until such time as it is reinstated by Mr. Murphy. Reinstatement will affect future payments only, with no retroactive amounts due. While not paid to Mr. Murphy, the amount of such CPI increase to Mr. Murphy's base salary will be retained for those provisions of his employment agreement that use a computation which includes the then existing level of base salary, including future CPI adjustments.

Item 6. Exhibits.

Exhibits:

31.1 Certifications of Chief Executive Officer Required by Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

31.2 Certifications of Chief Financial Officer Required by Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32 Certification of the Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

SIGNATURES

In accordance with the requirements of Section 13 or 15(d) 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.

Date: November 13, 2008

Date: November 13, 2008

PRO-DEX INC.
By: / s / Mark Murphy
Mark Murphy
Chief Executive Officer

PRO-DEX INC.
By: / s / Jeffrey J. Ritchey
Jeffrey J. Ritchey
Secretary and Chief Financial Officer

(Principal Financial and Accounting Officer)

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End of Filing