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

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**FORM 10-Q**

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(Mark One)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the quarterly period ended December 31, 2012

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

Commission File No.: 001-34839

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**Electromed, Inc.**

(Exact name of Registrant as specified in its charter)

**Minnesota**

(State or other jurisdiction of  
incorporation or organization)

**41-1732920**

(IRS Employer  
Identification No.)

**500 Sixth Avenue NW  
New Prague, MN 56071**

(Address of principal executive offices, including zip code)

**(952) 758-9299**

(Registrant's telephone number, including area code)

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer   
Non-accelerated filer

Accelerated filer   
Smaller Reporting Company

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

There were 8,114,252 shares of Electromed, Inc. common stock, par value \$0.01, outstanding as of the close of business on February 8, 2013.

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**Electromed, Inc.**  
**Index to Quarterly Report on Form 10-Q**

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**PART I – FINANCIAL INFORMATION****Item 1. Financial Statements****Electromed, Inc. and Subsidiary  
Condensed Consolidated Balance Sheets**

	December 31, 2012	June 30, 2012
<b>Assets</b>		
<b>Current Assets</b>	(Unaudited)	
Cash and cash equivalents	\$ 1,005,616	\$ 1,702,435
Accounts receivable (net of allowances for doubtful accounts of \$45,000)	9,725,142	10,850,859
Inventories	1,899,028	2,392,416
Prepaid expenses and other current assets	358,935	359,583
Income taxes receivable	605,744	340,744
Deferred income taxes	656,000	656,000
<b>Total current assets</b>	14,250,465	16,302,037
Property and equipment, net	3,481,373	3,170,014
Finite-life intangible assets, net	1,135,891	1,174,033
Other assets	276,582	274,940
<b>Total assets</b>	<u>\$ 19,144,311</u>	<u>\$ 20,921,024</u>
<b>Liabilities and Equity</b>		
<b>Current Liabilities</b>		
Revolving line of credit	\$ 600,000	\$ 1,768,128
Current maturities of long-term debt	66,191	254,020
Accounts payable	753,098	749,985
Accrued compensation	615,566	636,995
Warranty reserve	661,000	610,000
Other accrued liabilities	127,077	151,558
<b>Total current liabilities</b>	2,822,932	4,170,686
Long-term debt, less current maturities	1,356,961	1,390,003
Deferred income taxes	280,000	280,000
<b>Total liabilities</b>	4,459,893	5,840,689
Commitments and Contingencies (Note 7)		
<b>Equity</b>		
Common stock, \$0.01 par value; authorized: 13,000,000; shares issued and outstanding: 8,114,252 shares	81,143	81,143
Additional paid-in capital	13,045,518	12,959,136
Retained earnings	1,557,757	2,040,056
<b>Total equity</b>	14,684,418	15,080,335
<b>Total liabilities and equity</b>	<u>\$ 19,144,311</u>	<u>\$ 20,921,024</u>

See Notes to Condensed Consolidated Financial Statements.

[Table of Contents](#)**Electromed, Inc. and Subsidiary**  
**Condensed Consolidated Statements of Operations (Unaudited)**

	For the Three Months Ended December 31,		For the Six Months Ended December 31,	
	2012	2011	2012	2011
Net revenues	\$ 3,856,370	\$ 4,790,344	\$ 7,887,656	\$ 10,169,262
Cost of revenues	1,342,002	1,309,064	2,552,455	2,618,631
<b>Gross profit</b>	<u>2,514,368</u>	<u>3,481,280</u>	<u>5,335,201</u>	<u>7,550,631</u>
Operating expenses				
Selling, general and administrative	3,000,532	3,130,799	5,816,544	6,530,602
Research and development	109,250	250,339	210,440	467,425
<b>Total operating expenses</b>	<u>3,109,782</u>	<u>3,381,138</u>	<u>6,026,984</u>	<u>6,998,027</u>
<b>Operating income (loss)</b>	(595,414)	100,142	(691,783)	552,604
Interest expense, net of interest income of \$10,975, \$1,634, \$15,322, and \$3,662 respectively	25,777	43,588	62,516	87,511
<b>Net income (loss) before income taxes</b>	(621,191)	56,554	(754,299)	465,093
Income tax benefit (expense)	210,000	(32,000)	272,000	(195,000)
<b>Net income (loss)</b>	<u>\$ (411,191)</u>	<u>\$ 24,554</u>	<u>\$ (482,299)</u>	<u>\$ 270,093</u>
Earnings (loss) per share:				
Basic and diluted	<u>\$ (0.05)</u>	<u>\$ 0.00</u>	<u>\$ (0.06)</u>	<u>\$ 0.03</u>
Weighted-average common shares outstanding:				
Basic	<u>8,114,252</u>	<u>8,101,745</u>	<u>8,114,252</u>	<u>8,101,330</u>
Diluted	<u>8,114,252</u>	<u>8,125,458</u>	<u>8,114,252</u>	<u>8,121,971</u>

See Notes to Condensed Consolidated Financial Statements.

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**Condensed Consolidated Statements of Cash Flows (Unaudited)**

	For the Six Months Ended	
	December 31,	
	2012	2011
<b>Cash Flows From Operating Activities</b>		
Net income (loss)	\$ (482,299)	\$ 270,093
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation	231,918	193,790
Amortization of finite-life intangible assets	66,234	60,199
Amortization of debt issuance costs	6,377	6,066
Share-based compensation expense	86,382	62,108
Loss on disposal of property and equipment	22,020	9,865
Changes in operating assets and liabilities:		
Accounts receivable	1,125,717	(1,111,600)
Inventories	493,388	(541,677)
Prepaid expenses and other assets	(272,371)	(138,627)
Accounts payable and accrued liabilities	(74,972)	(343,091)
<b>Net cash provided by (used in) operating activities</b>	<u>1,202,394</u>	<u>(1,532,874)</u>
<b>Cash Flows From Investing Activities</b>		
Expenditures for property and equipment	(482,122)	(618,966)
Expenditures for finite-life intangible assets	(28,092)	(22,650)
<b>Net cash used in investing activities</b>	<u>(510,214)</u>	<u>(641,616)</u>
<b>Cash Flows From Financing Activities</b>		
Net payments on revolving line of credit	(1,168,128)	—
Principal payments on long-term debt including capital lease obligations	(220,871)	(189,056)
Payments of deferred financing fees	—	(10,526)
Proceeds from warrant exercises	—	5,301
Proceeds from subscription notes receivable	—	22,500
<b>Net cash used in financing activities</b>	<u>(1,388,999)</u>	<u>(171,781)</u>
<b>Net decrease in cash and cash equivalents</b>	<u>(696,819)</u>	<u>(2,346,271)</u>
Cash and cash equivalents		
Beginning of period	1,702,435	4,091,739
End of period	<u>\$ 1,005,616</u>	<u>\$ 1,745,468</u>

See Notes to Condensed Consolidated Financial Statements.

**Electromed, Inc. and Subsidiary**  
**Notes to Condensed Consolidated Financial Statements**  
**(Unaudited)**

**Note 1. Interim Financial Reporting**

**Basis of presentation:** Electromed, Inc. (the Company) develops, manufactures and markets innovative airway clearance products which apply High Frequency Chest Wall Oscillation (HFCWO) therapy in pulmonary care for patients of all ages. The Company markets its products in the United States to the home health care and institutional markets for use by patients in personal residences, hospitals and clinics. The Company also sells internationally both directly and through distributors. Since its inception, the Company has operated in a single industry segment: developing, manufacturing and marketing medical equipment.

The accompanying unaudited condensed consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial statements and pursuant to the rules and regulations of the Securities and Exchange Commission. In the opinion of management, the accompanying unaudited condensed consolidated financial statements reflect all adjustments consisting of normal recurring adjustments necessary for a fair presentation of the Company's financial position and results of operations as required by Regulation S-X, Rule 10-01. Interim results of operations are not necessarily indicative of the results that may be achieved for the full year. The financial statements and related notes do not include all information and footnotes required by accounting principles generally accepted in the United States of America for annual reports. This interim report should be read in conjunction with the consolidated financial statements included in the Company's annual report on Form 10-K for the year ended June 30, 2012.

The Company has evaluated subsequent events and transactions for potential recognition or disclosure in the financial statements through the date the consolidated financial statements are issued.

**Principles of consolidation:** The accompanying condensed consolidated financial statements include the accounts of Electromed, Inc. and its subsidiary, Electromed Financial, LLC. Operating activities and net assets in Electromed Financial, LLC were insignificant as of and for the three and six months ended December 31, 2012 and the year ended June 30, 2012.

**A summary of the Company's significant accounting policies follows:**

**Use of estimates:** Management uses estimates and assumptions in preparing the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported revenues and expenses. Actual results could vary from the estimates that were used. The Company believes the critical accounting policies that require the most significant assumptions and judgments in the preparation of its consolidated financial statements include: revenue recognition and the estimation of selling price adjustments, allowance for doubtful accounts, inventory obsolescence, share-based compensation, warranty reserve and income taxes.

**Net income (loss) per common share:** Net income (loss) is presented on a per share basis for both basic and diluted common shares. Basic net income (loss) per common share is computed using the weighted average number of common shares outstanding during the period. The diluted net income (loss) per common share calculation assumes that all stock warrants were exercised and converted into common stock at the beginning of the period, unless their effect would be anti-dilutive. Common stock equivalents of 624,900 and 537,800 were excluded from the calculation of diluted earnings per share for the six months ended December 31, 2012 and 2011, respectively, as their impact was antidilutive.

**Reclassifications:** Certain items in the fiscal 2012 financial statements have been reclassified to be consistent with the classifications adopted for fiscal 2013. The fiscal 2012 reclassifications had no impact on previously reported net income or shareholders' equity.

[Table of Contents](#)**Note 2. Inventories**

The components of inventory were approximately as follows:

	December 31, 2012	June 30, 2012
Parts inventory	\$ 1,140,000	\$ 1,397,000
Work in process	212,000	81,000
Finished goods	577,000	944,000
Less: Reserve for obsolescence	(30,000)	(30,000)
Total	<u>\$ 1,899,000</u>	<u>\$ 2,392,000</u>

**Note 3. Finite-Life Intangible Assets**

The carrying value of patents and trademarks includes the original cost of obtaining the patents, periodic renewal fees, and other costs associated with maintaining and defending patent and trademark rights. Patents and trademarks are amortized over their estimated useful lives, generally 15 and 12 years, respectively. Accumulated amortization was approximately \$415,000 and \$352,000 at December 31, 2012 and June 30, 2012, respectively.

The activity and balances of finite-life intangible assets were approximately as follows:

	Six Months Ended December 31, 2012	Year Ended June 30, 2012
Balance, beginning	\$ 1,174,000	\$ 1,236,000
Additions	28,000	62,000
Amortization expense	(66,000)	(124,000)
Balance, ending	<u>\$ 1,136,000</u>	<u>\$ 1,174,000</u>

**Note 4. Warranty Liability**

The Company provides a lifetime warranty on its products to the prescribed patient for sales within the United States and Canada, a five-year warranty on its products to the prescribed patient for sales within Greece, and a three-year warranty for all institutional sales and sales to individuals outside the United States, Canada and Greece. The Company estimates the costs that may be incurred under its warranty and records a liability in the amount of such costs at the time the product is shipped. Factors that affect the Company's warranty liability include the number of units shipped, historical and anticipated rates of warranty claims, and cost per claim. The Company periodically assesses the adequacy of its recorded warranty liability and adjusts the amounts as necessary.

Changes in the Company's warranty liability were approximately as follows:

	Six Months Ended December 31, 2012	Year Ended June 30, 2012
Beginning warranty reserve	\$ 610,000	\$ 444,000
Accrual for products sold	176,000	351,000
Expenditures and costs incurred for warranty claims	(125,000)	(185,000)
Ending warranty reserve	<u>\$ 661,000</u>	<u>\$ 610,000</u>

**Note 5. Income Taxes**

On a quarterly basis, the Company estimates what its effective tax rate will be for the full fiscal year and records a quarterly income tax provision based on the anticipated rate. As the year progresses, the Company refines its estimate based on the facts and circumstances by each tax jurisdiction. The effective tax rate for the six months ended December 31, 2012 and 2011 was 36.1% and 41.9%, respectively.

**Note 6. Financing Arrangements and Subsequent Event**

The Company has a credit facility that provides for term loans and a revolving line of credit of \$6,000,000, as of December 31, 2012. The line of credit expires on December 31, 2013, if not renewed. Advances are due at the expiration date and are secured by substantially all Company assets. Interest on advances accrue at LIBOR plus 3.08% (3.33% at December 31, 2012) and is payable monthly. The amount available for borrowing is limited to 60% of eligible accounts receivable. The Company's credit facility contains certain financial and nonfinancial covenants and restricts the payment of dividends. The Company was in violation of certain of these covenants during the period ended December 31, 2012.

The Company notified the bank of its violations of the covenants, and, on February 13, 2013, the Company and the bank entered into a Waiver and Fourth Amendment to Credit Agreement, pursuant to which the bank has waived the events of default. The Waiver and Fourth Amendment to Credit Agreement provides for adjustments to the financial covenants through September 30, 2013, a decrease in the revolving line of credit to \$2,500,000, and an adjustment to the interest rate to LIBOR plus 3.50%.

**Note 7. Commitments and Contingencies**

The Company is occasionally involved in claims and disputes arising in the ordinary course of business. The Company insures its business risks where possible to mitigate the financial impact of individual claims, and establishes reserves for an estimate of any probable cost of settlement or other disposition.

**Note 8. Related Parties**

The Company uses a parts supplier whose founder and president became a director of the Company during fiscal year 2011, and is currently chairman of the Company's board of directors. For the six months ended December 31, 2012 and 2011, the Company made payments to the supplier of approximately \$209,000 and \$324,000, respectively.



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

*Some of the statements in this report may contain forward-looking statements made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 that reflect our current view on future events, future business, industry and other conditions, our future performance, and our plans and expectations for future operations and actions. In some cases, you can identify forward-looking statements by the following words: anticipate, believe, continue, could, estimate, expect, intend, may, ongoing, plan, potential, predict, project, should, will, would, or the negative of these terms or other comparable terminology, although not all forward-looking statements contain these words. Our forward-looking statements in this report primarily relate to the following: our ability to gain market share; our expectations regarding the recording of tax credits; our expectations regarding leveraging manufacturing costs and its effect on gross profit percentage; our expected business strategy and the impact of our business strategy on revenues and earnings, including the expected contributions of new members of our sales staff; expected expenditures for research and development; our expectations regarding capital expenditures; and our beliefs regarding the sufficiency of working capital and our ability and intention to renew or obtain financing. These statements involve known and unknown risks, uncertainties and other factors that may cause our results or our industry's actual results, levels of activity, performance or achievements to be materially different from the information expressed or implied by these forward-looking statements. Forward-looking statements are only predictions and are not guarantees of performance. These statements are based on our management's beliefs and assumptions, which in turn are based on currently available information.*

*You should read this report thoroughly with the understanding that our actual results and actions may differ materially from those set forth in the forward-looking statements for many reasons, including events beyond our control and assumptions that prove to be inaccurate or unfounded. Our actual results or actions could and likely will differ materially from those anticipated in the forward-looking statements for many reasons, including the reasons described in this report. These factors include, but are not limited to: the competitive nature of our market; the risks associated with expansion into international markets; changes to Medicare, Medicaid, or private insurance reimbursement policies; changes to health care laws; changes affecting the medical device industry; our need to maintain regulatory compliance and to gain future regulatory approvals and clearances; our ability to recruit, train and retain an effective sales force, reimbursement staff, and patient services staff; our ability to protect our intellectual property; the effect of pending and potential future litigation, including legal expenses, which may arise, including with respect to our intellectual property or otherwise; the impact of tight credit markets on our ability to continue to obtain financing on reasonable terms; and general economic and business conditions.*

### Overview

Electromed, Inc. (we, us, our, the Company, or Electromed) was incorporated in 1992. We are engaged in the business of providing innovative airway clearance products applying High Frequency Chest Wall Oscillation (HFCWO) therapy in pulmonary care for patients of all ages.

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We manufacture, market and sell products that provide HFCWO, including the Electromed, Inc. SmartVest® Airway Clearance System (SmartVest System) and related products, to patients with compromised mucus clearance function. The products are sold for both the home health care market and the institutional market for use by patients in hospitals, which are referred to as “institutional sales.” For approximately ten years, we have marketed the SmartVest System and its predecessor products to patients suffering from cystic fibrosis, bronchiectasis (including chronic bronchitis or chronic obstructive pulmonary disease (COPD) that has resulted in a diagnosis of bronchiectasis), or any one of certain enumerated neuro-muscular diseases, and can demonstrate that another less expensive physical or mechanical treatment did not adequately mobilize retained secretions. Additionally, we offer such products upon physician prescription to a patient population that includes post-surgical and intensive care patients, patients with end-stage neuromuscular disease, and ventilator-dependent patients. Our goal is to be a consistent innovator in providing HFCWO to patients with impaired pulmonary function.

### Critical Accounting Policies and Estimates

Our significant accounting policies and estimates are disclosed in Part II, Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” and Note 1 to our Audited Consolidated Financial Statements, included in Part II, Item 8, of our Annual Report on Form 10-K for the fiscal year ended June 30, 2012. The critical accounting policies used in the preparation of the consolidated financial statements as of and for the three and six month periods ended December 31, 2012, have remained unchanged from June 30, 2012.

Some of our accounting policies require us to exercise significant judgment in selecting the appropriate assumptions for calculating financial statements. Such judgments are subject to an inherent degree of uncertainty. These judgments are based upon our historical experience, known trends in our industry, terms of existing contracts and other information from outside sources, as appropriate. We believe the critical accounting policies that require the most significant assumptions and judgments in the preparation of its consolidated financial statements include: revenue recognition and the estimation of selling price adjustments, allowance for doubtful accounts, inventory obsolescence, share-based compensation, income taxes, and warranty liability.

### Results of Operations

#### *Three Months Ended December 31, 2012 Compared to Three Months Ended December 31, 2011*

#### *Revenues*

Revenue results for the three month periods are summarized in the table below (dollar amounts in thousands).

	Three Months Ended December 31,		Increase (Decrease)	
	2012	2011		
<b>Total Revenue</b>	\$ 3,856	\$ 4,790	\$ (934)	(19.5)%
<b>Home Care Revenue</b>	\$ 3,328	\$ 4,298	\$ (970)	(22.6)%
<b>International Revenue</b>	\$ 208	\$ 192	\$ 16	8.3%
<b>Government/Institutional Revenue</b>	\$ 320	\$ 300	\$ 20	6.7%

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*Home Care Revenue.* Home care revenue was approximately \$3,328,000 for the three months ended December 31, 2012, representing a decrease of approximately \$970,000, or 22.6%, compared to the same period in 2011. The decrease in revenue was caused by downward pressure on pricing and added administrative procedures implemented by third party payers in the insurance claims process which has lengthened the approval process compared to the prior year.

*International Revenue.* International revenue was approximately \$208,000 for the three months ended December 31, 2012, representing an increase of approximately \$16,000, or 8.3%, compared to the same period in 2011. This increase resulted primarily from an increase in sales to the Middle East, which were offset by a decrease in sales to Europe and Asia during the quarter ended December 31, 2012, as compared to the same period in 2011. International sales can be affected by the timing of distributor purchases and cause fluctuation regionally on a quarterly basis. Management continues to explore international opportunities in growth markets while focusing on domestic sales growth. Subsequent to the end of the second quarter, we hired a full-time employee to manage international sales.

*Government/Institutional Revenue.* Government/institutional revenue was approximately \$320,000 for the three months ended December 31, 2012, representing an increase of approximately \$20,000, or 6.7%, compared to approximately \$300,000 during the same period in 2011. This resulted from an increase in sales to distributors, group purchasing organization (GPO) members, and other institutions of \$37,000, from approximately \$221,000 in the three months ended December 31, 2011 to approximately \$258,000 in the comparable period in the current year. The increase in Institutional sales was offset by a \$15,000 decrease in sales to the U.S. Department of Veterans Affairs and other government entities which decreased to approximately \$64,000 for the three months ended December 31, 2012, from approximately \$79,000 during the same period the prior year. The increase in Institutional and Governmental sales was the result of continued efforts of our sales force.

### ***Gross Profit***

Gross profit decreased to approximately \$2,514,000, or 65.2% of net revenues, for the three months ended December 31, 2012, from approximately \$3,481,000, or 72.7% of net revenues, in the same period in 2011. The decrease in gross profit percentage was primarily the result of reduced leverage of manufacturing costs on lower revenue levels. We believe that as we grow sales we will be able to leverage manufacturing costs more effectively and margins will return to more historical levels above 70%.

### ***Operating expenses***

*Selling, general and administrative expenses.* Selling, general and administrative (SG&A) expenses were approximately \$3,001,000 for the three months ended December 31, 2012, representing a decrease of approximately \$130,000, or 4.2%, compared to SG&A expenses of approximately \$3,131,000 for the same period the prior year. Payroll and compensation-related expenses were approximately \$1,459,000 for the three months ended December 31, 2012, representing a decrease of approximately \$37,000, or 2.5%, compared to approximately \$1,496,000 in the same period the prior year.

Travel, meals and entertainment, and trade show expenses were approximately \$333,000 in the three months ended December 31, 2012, representing a decrease of approximately \$131,000, or 28.2%, compared to approximately \$464,000 in the same period in the prior year. This decrease was primarily due to the elimination of industry training that was sponsored by Electromed, eliminating costs related to tradeshows that do not fit our growth strategies and reducing travel expenses among the sales force through improved travel planning.

Advertising and marketing expenses for the three months ended December 31, 2012 were approximately \$152,000, a decrease of approximately \$156,000, or 50.6%, compared to approximately \$308,000 in the same period the prior year. The decrease was related to bringing marketing leadership in-house, thus reducing our external marketing fees, as well as targeting more cost-effective advertising.

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Professional fees for the three months ended December 31, 2012 were approximately \$356,000, an increase of approximately \$161,000 compared to approximately \$195,000 in the same period in the prior year. These fees are for services related to legal costs, reporting requirements, expenses related to information technology security and backup, one time consulting expenses, and expenses for printing and other shareowner services. The increase in fees over the same period last year was primarily due to a shareholder's proposal at our annual meeting and the resulting litigation brought by the Company, as well as consulting fees related to upgrading our current information technology infrastructure.

*Research and development expenses.* Research and development expenses were approximately \$109,000 for the three months ended December 31, 2012, representing a decrease of approximately \$141,000, or 56.4%, compared to approximately \$250,000 in the same period the prior year. Approximately \$90,000 of the decrease was a result of discontinuing the use of a certain outside vendor based on project needs. Research and development expenses for the three months ended December 31, 2012 were 2.8% of revenue, compared to 5.2% of revenue in the same period the prior year. As a percentage of sales, management expects to spend approximately 5.0% of sales on research and development expenses over the long term.

### ***Interest expense***

Interest expense was approximately \$37,000 for the three months ended December 31, 2012, representing a decrease of approximately \$8,000, or 17.8%, compared to approximately \$45,000 for the same period the prior year. The decrease resulted from a decrease in average debt outstanding.

### ***Income tax benefit (expense)***

Income tax benefit is estimated at approximately \$210,000 for the three months ended December 31, 2012, compared to income tax expense of \$32,000 in the same period in the prior year. The effective tax rates for the three months ended December 31, 2012 and 2011 were 33.8% and 56.6%, respectively. On a quarterly basis, management estimates what its effective tax rate will be for the full fiscal year and records a quarterly income tax provision based on the anticipated rate. As the year progresses, the estimate is refined based on the facts and circumstances by each tax jurisdiction. The decrease in effective tax rate is related primarily to permanent differences including certain meals and entertainment expenses that are only 50% deductible for tax purposes as well as the estimate for the Federal Research and Development Tax Credit which was not extended until January 2013 by the U.S. Congress. The effect of the estimated tax credit will be recorded in the quarter ended March 31, 2013.

### ***Net income (loss)***

Net loss for the three months ended December 31, 2012 was approximately \$411,000 compared to net income of approximately \$25,000 for the same period in the prior year. The decrease in net income primarily resulted from a decrease in sales volume partially offset by decreases in expenses. Management continues to believe certain investments currently being made are creating the platform for profitable sales growth. During the quarter ended December 31, 2012, management has completed a realignment of sales territories and instituted a new compensation plan for the sales force designed to drive future sales growth. Management is focused on controlling costs more aggressively short term while implementing key strategies for growth which includes full staffing of our U.S. sales regions, updated branding including a new logo, marketing material, and developing more distributors internationally by hiring an international sales manager.

**Six Months Ended December 31, 2012 Compared to Six Months Ended December 31, 2011****Revenues**

Revenue results for the six month periods are summarized in the table below (dollar amounts in thousands).

	Six Months Ended December 31,		Increase (Decrease)	
	2012	2011		
<b>Total Revenue</b>	\$ 7,888	\$ 10,169	\$ (2,281)	(22.4)%
<b>Home Care Revenue</b>	\$ 6,902	\$ 9,430	\$ (2,528)	(26.8)%
<b>International Revenue</b>	\$ 317	\$ 229	\$ 88	38.4%
<b>Government/Institutional Revenue</b>	\$ 669	\$ 510	\$ 159	31.2%

*Home Care Revenue.* Home care revenue was approximately \$6,902,000 for the six months ended December 31, 2012, representing a decrease of approximately \$2,528,000, or 26.8%, compared to the same period in 2011. The decrease in revenue was caused by downward pressure on pricing and added administrative procedures implemented by third party payers in the insurance claims process which has lengthened the approval process compared to the prior year. The decrease in revenues also reflects a decrease in the existing sales staff from 26 full time equivalents in the six months ended December 31, 2011, to 24.5 in the same period in the current year as well as turnover in Clinical Area Managers (CAMs) of approximately 30%, or seven CAMs, during the twelve months ended December 31, 2012.

*International Revenue.* International revenue was approximately \$317,000 for the six months ended December 31, 2012, representing an increase of approximately \$88,000, or 38.4%, compared to the same period in 2011. This increase resulted primarily from an increase in sales to the Middle East. Management continues to explore international opportunities in growth markets while focusing on domestic sales growth.

*Government/Institutional Revenue.* Government/institutional revenue was approximately \$669,000 for the six months ended December 31, 2012, representing an increase of approximately \$159,000, or 31.2%, compared to approximately \$510,000 during the same period in 2011. This resulted from a \$145,000 increase in sales to distributors, group purchasing organization (GPO) members, and other institutions which increased to approximately \$544,000 for the six months ended December 31, 2012, from approximately \$399,000 during the same period the prior year. Sales to the U.S. Department of Veterans Affairs and other government entities also increased by approximately \$14,000, to \$125,000 for the six months ended December 31, 2012, compared to \$111,000 for the same period in 2011. The increase in government/institutional sales is due to the efforts of our sales force continuing to produce higher sales in these categories.

**Gross Profit**

Gross profit decreased to approximately \$5,335,000, or 67.6% of net revenues, for the six months ended December 31, 2012, from approximately \$7,551,000, or 74.2% of net revenues, in the same period in 2011. The decrease in gross profit percentage was primarily the result of reduced leverage of manufacturing costs on lower revenue levels. We believe that as we grow sales we will be able to leverage manufacturing costs more effectively and margins will return to more historical levels above 70%.

***Operating expenses***

*Selling, general and administrative expenses.* Selling, general and administrative expenses were approximately \$5,817,000 for the six months ended December 31, 2012, representing a decrease of approximately \$714,000, or 10.9%, compared to SG&A expenses of approximately \$6,531,000 for the same period the prior year. Payroll and compensation-related expenses were approximately \$2,794,000 for the six months ended December 31, 2012, representing a decrease of approximately \$327,000, or 10.5%, compared to approximately \$3,121,000 in the same period the prior year. This decrease was primarily a result of lower incentive compensation for the CAMs which is correlated with revenue levels, as well as a reduction of overall management compensation as compared to the same period in the prior year.

Travel, meals and entertainment and trade show expenses were approximately \$724,000 in the six months ended December 31, 2012, representing a decrease of approximately \$214,000, or 22.8%, compared to approximately \$938,000 in the same period in the prior year. This decrease was primarily due to the elimination of industry training that was sponsored by Electromed, eliminating costs related to tradeshows that do not fit our growth strategies and reducing travel expenses among the sales force through improved travel planning.

Advertising and marketing expenses for the six months ended December 31, 2012 were approximately \$334,000, a decrease of approximately \$327,000, or 49.5%, compared to approximately \$661,000 in the same period the prior year. These decreased expenditures related to bringing marketing leadership in-house, thus reducing our external marketing fees, as well as targeting more cost-effective advertising.

Professional fees for the six months ended December 31, 2012 were approximately \$561,000, an increase of approximately \$53,000 compared to approximately \$508,000 in the same period in the prior year. These fees are for services related to legal costs, reporting requirements, expenses related to information technology security and backup, one time consulting expenses, and expenses for printing and other shareowner services. The increase in fees over the same period last year was primarily due to a shareholder's proposal at our annual meeting and the resulting litigation brought by the Company, as well as consulting fees related to upgrading our current information technology infrastructure.

*Research and development expenses.* Research and development expenses were approximately \$210,000 for the six months ended December 31, 2012, representing a decrease of approximately \$257,000, or 55.0%, compared to approximately \$467,000 in the same period the prior year. Approximately \$180,000 of the decrease was a result of discontinuing the use of a certain outside vendor based on project needs. Research and development expenses for the six months ended December 31, 2012 were 2.7% of revenue, compared to 4.6% of revenue in the same period the prior year. As a percentage of sales, management expects to spend approximately 5.0% of sales on research and development expenses over the long term.

***Interest expense***

Interest expense was approximately \$78,000 for the six months ended December 31, 2012, representing a decrease of approximately \$13,000, or 14.3%, compared to approximately \$91,000 for the same period the prior year. The decrease resulted from a decrease in average debt outstanding.

***Income tax benefit (expense)***

Income tax benefit is estimated at approximately \$272,000 for the six months ended December 31, 2012 compared to income tax expense of approximately \$195,000 in the same period in the prior year. The effective tax rates for the six months ended December 31, 2012 and December 31, 2011 were 36.1% and 41.9%, respectively. On a quarterly basis, management estimates what its effective tax rate will be for the full fiscal year and records a quarterly income tax provision based on the anticipated rate. As the year progresses, the estimate is refined based on the facts and circumstances by each tax jurisdiction. The decrease in effective tax rate is related primarily to permanent differences including certain meals and entertainment expenses that are only 50% deductible for tax purposes as well as the estimate for the Federal Research and Development Tax Credit which was not extended until January 2013, by the U.S. Congress. The effect of the estimated tax credit will be recorded in the quarter ended March 31, 2013.

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*Net income (loss)*

Net loss for the six months ended December 31, 2012 was approximately \$482,000 compared to net income of approximately \$270,000 for the same period the prior year. The decrease in net income primarily resulted from a decrease in sales volume partially offset by decreases in expenses. Management continues to believe certain investments currently being made are creating the platform for profitable sales growth. During the quarter ended December 31, 2012, management completed a realignment of sales regions. Management is focused on controlling costs more aggressively short term while implementing key strategies for growth which includes full staffing of our U.S. sales regions, updated branding including a new logo, marketing material, and developing more distributors internationally by hiring an international sales manager.

**Liquidity and Capital Resources**

*Cash Flows and Sources of Liquidity*

*Cash Flows from Operating Activities*

For the six months ended December 31, 2012, net cash provided by operating activities was approximately \$1,202,000. Cash flows provided by operations consisted of approximately \$482,000 in net loss, adjusted for non-cash expenses of approximately \$413,000, offset by decreases in accounts receivable and inventory of \$1,126,000 and \$493,000, respectively, and increases in prepaid expenses and other assets of \$272,000. In addition, accounts payable and accrued liabilities decreased approximately \$75,000.

For the six months ended December 31, 2011, net cash used in operating activities was approximately \$1,533,000. Cash flows used by operations consisted of approximately \$270,000 in net income, adjusted for non-cash expenses of approximately \$332,000, offset by increases in accounts receivable, inventory, and prepaid expenses and other assets of \$1,112,000, \$542,000, and \$139,000, respectively. In addition, accounts payable and accrued liabilities decreased approximately \$343,000.

*Cash Flows from Investing Activities*

For the six months ended December 31, 2012, cash used in investing activities was approximately \$510,000. During this period we paid approximately \$482,000 for purchases of property and equipment. We also paid approximately \$28,000 for patent related costs.

For the six months ended December 31, 2011, cash used in investing activities was approximately \$642,000. During this period we paid approximately \$619,000 for purchases of property and equipment, including \$414,000 for converting approximately 10,000 square feet of a newly leased building to office space. We also paid approximately \$23,000 for patent related costs.

*Cash Flows from Financing Activities*

For the six months ended December 31, 2012, cash used in financing activities was approximately \$1,389,000, which consisted of principal payments on long-term debt of \$221,000, and payments on our revolving line of credit of \$1,168,000.

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For the six months ended December 31, 2011, cash used in financing activities was approximately \$172,000. We received approximately \$28,000 from warrant exercises and receipts on subscription notes receivable, offset by principal payments on long-term debt of approximately \$189,000 and payments of deferred financing fees of approximately \$11,000.

### ***Adequacy of Capital Resources***

Based on our current operational performance, we believe our cash and available borrowings under the existing credit facility will provide adequate liquidity for the next year. However, we cannot guarantee that we will be able to procure additional financing upon favorable terms, if at all.

Our primary capital requirements relate to adding employees in our sales force and supporting functions; continuing research and development efforts; and for general corporate purposes, including to finance equipment purchases and other capital expenditures in the ordinary course of business and to satisfy working capital needs.

For the first six months of fiscal years 2013 and 2012, we spent approximately \$482,000 and \$619,000 on property and equipment, respectively. We currently expect to finance equipment purchases with borrowings under our credit facility and cash flows from operations. We may need to incur additional debt or equity financing if we have an unforeseen need for additional capital equipment or if our operating performance does not generate adequate cash flows.

On November 8, 2011 we entered into an amended and restated credit facility with U.S. Bank, National Association (U.S. Bank), which was amended on December 30, 2011, May 14, 2012, September 21, 2012, and February 13, 2013, that provides for a revolving line of credit of \$2,500,000, and \$2,520,000 in term debt. A \$1,520,000 Term Loan bears interest at 5.79% (Term Loan A). The remaining \$1,000,000 term loan bore interest at 4.28% (Term Loan B) and was paid in full during October 2012. Interest on the operating line of credit accrues at LIBOR plus 3.50% (3.75% at February 13, 2013, the date of the most recent amendment) and is payable monthly. The amount eligible for borrowing on the line of credit is limited to 60% of eligible accounts receivable. The line of credit will expire on December 31, 2013, if not earlier renewed. Term Loan A requires monthly payments of principal and interest of approximately \$10,700 and has a maturity date of December 9, 2014. As of December 31, 2012, we had \$600,000 outstanding on the operating line of credit and approximately \$1,385,000 outstanding on Term Loan A for a total amount outstanding under the U.S. Bank credit facility of \$1,985,000. As of the most recent amendment date of February 13, 2013, we had \$600,000 outstanding on the operating line of credit and net unused availability of \$1,900,000. We are required to pay a fee of 0.125% per annum on unused portions of the revolving line of credit.

Our credit facility contains certain financial and nonfinancial covenants, which, among others, required the Company to maintain a certain fixed charge coverage ratio and a maximum cash flow leverage ratio, and restricts the payment of dividends. We were in violation of certain financial and nonfinancial covenants during the period ended December 31, 2012. On February 13, 2013, we entered into a Waiver and Fourth Amendment to our Credit Agreement with U.S. Bank (the "Waiver Agreement"). See Part II, Item 5 to this quarterly report for a description of the material terms of such Waiver Agreement.

### **Certain Information Concerning Off-Balance Sheet Arrangements**

We have no off-balance sheet arrangements.

### **Item 3. Quantitative and Qualitative Disclosure About Market Risk**

As a smaller reporting company, we are not required to provide disclosure pursuant to this item.



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

### **Evaluation of Disclosure Controls and Procedures**

Our principal executive officer and principal financial officer evaluated the effectiveness of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934 (the "Exchange Act"), as of the end of the period subject to this Report. Based on this evaluation, our principal executive officer and principal financial officer concluded that our disclosure controls and procedures were effective.

### **Changes to Internal Control Over Financial Reporting**

There were no changes in our internal control over financial reporting that occurred during the three months ended December 31, 2012 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## **PART II. OTHER INFORMATION**

### **Item 1. Legal Proceedings**

Occasionally, we may be party to legal actions, proceedings, or claims in the ordinary course of business, including claims based on assertions of patent and trademark infringement. Corresponding costs are accrued when it is probable that loss will be incurred and the amount can be precisely or reasonably estimated.

On December 7, 2012, we instituted a lawsuit in the District Court for Scott County, Minnesota against Eileen Manning, the proponent of a shareholder proposal at the Company's 2012 Annual Meeting of Shareholders (the "Annual Meeting") seeking to elect two individuals to the Company's board of directors, and Robert D. Hansen, the Company's former Chairman and Chief Executive Officer. The Company asserts that Ms. Manning, the owner of an entity that formerly provided marketing services to the Company, violated the proxy solicitation rules in connection with the nomination and election of directors at the Annual Meeting. Ms. Manning has asserted a counterclaim alleging that the Company has violated her rights as a shareholder by failing to count and certify the results of the election. The Company also asserts that Mr. Hansen violated his Separation Agreement and Release in connection with his actions relating to Ms. Manning's proposal prior to and at the Annual Meeting and seeks declaratory relief and damages. Mr. Hansen has asserted a counterclaim alleging that the Company breached the Separation Agreement and Release by failing to make a payment under the agreement.

### **Item 1A. Risk Factors**

As a smaller reporting company, we are not required to provide disclosure pursuant to this item.

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

None.

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

None.

### **Item 4. Mine Safety Disclosures**

None.

## **Item 5. Other Information**

On February 13, 2013, the Company entered into a Waiver and Fourth Amendment to Credit Agreement (the "Waiver Agreement") with U.S. Bank National Association (the "Bank"), pursuant to which the Bank waived certain covenant violations by the Company under its Amended and Restated Credit Agreement with the Bank, dated as of November 7, 2011, as amended (the "Credit Agreement"). Amongst other things, the Credit Agreement, as amended prior to the Waiver Agreement, forbid the Company from (1) permitting its fixed charge coverage ratio as of the last day of any fiscal quarter for the four consecutive fiscal quarters ending on such date to be less than 1.2 to 1.0 and (2) permitting its total cash flow leverage ratio as of the last day of any fiscal quarter for the four consecutive fiscal quarters ending on such date to be more than 3.5 to 1.0. In addition, the Credit Agreement requires that the Company's chief executive officer position may not change without the Bank's consent. The Company was in violation of the aforementioned financial covenants as of December 31, 2012 and the covenant regarding the chief executive officer position as of December 1, 2012.

Pursuant to the Waiver Agreement, the Bank agreed to waive the specific covenant violations provided above as events of default under the Credit Agreement. In addition, the Waiver Agreement: (1) revised the definition of Applicable Margin from 3.08% to 3.50%; (2) revised the definition of Fixed Charge Coverage Ratio to remove from the numerator references to certain severance expenses made, and related tax expenses accrued, by the Company during the fiscal quarters ended December 31, 2011 and June 30, 2012; (3) revised the definition of Revolving Commitment Amount from \$6,000,000 to \$2,500,000; (4) amended the Company's financial reporting covenant to provide unaudited financial statements on a monthly basis instead of a quarterly basis and to require the Company to provide summaries of referrals and product shipments each month; (5) revised the definition of permitted indebtedness to exclude certain subordinated debt that was previously permitted; (6) revised the definition of fixed charge coverage ratio to decrease the ratio from 1.2 to 1.0 (measured on a quarterly basis using the four consecutive quarters ending on such date) to 1.15 to 1.0 for the quarter ending September 30, 2013 (measured only on such date and only for such quarter); (7) amended the total cash flow leverage ratio covenant to replace the ratio entirely with a minimum EBITDA covenant that forbids the Company from having EBITDA of less than negative \$275,000 for the quarter ending March 31, 2013 and \$425,000 for the quarter ending June 30, 2013; (8) eliminated the key man life insurance policy covenant; and (9) amended the form of compliance certificate set forth in the Credit Agreement to conform it with the aforementioned changes. The Company also released claims against the Bank, reasserted its representations and warranties under the Credit Agreement, and reaffirmed the Credit Agreement and related loan and security documents.

The foregoing summary does not purport to be complete and is qualified in its entirety by reference to the full text of the Waiver Agreement, which is filed as Exhibit 10.3 to this quarterly report on Form 10-Q.

## **Item 6. Exhibits**

See attached exhibit index.

## SIGNATURES

Pursuant to 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: February 14, 2013

ELECTROMED, INC.

/s/ Kathleen S. Skarvan

Kathleen S. Skarvan, Chief Executive Officer  
(Principal Executive Officer)

/s/ Jeremy T. Brock

Jeremy T. Brock, Chief Financial Officer  
(Principal Financial Officer and Principal Accounting Officer)

**EXHIBIT INDEX  
ELECTROMED, INC.  
FORM 10-Q**

<b>Exhibit Number</b>	<b>Description</b>
10.1	Waiver Agreement by and between the Company and U.S. Bank, National Association, dated November 13, 2012.
10.2*	Amended and Restated Employment Agreement by and between the Company and Jeremy T. Brock, dated November 15, 2012.
10.3	Waiver and Fourth Amendment to Credit Agreement by and between the Company and U.S. Bank, National Association, dated February 13, 2013.
10.4*	Employment Agreement dated effective December 1, 2012, by and between the Company and Kathleen Skarvan (incorporated by reference to the Company's current report on Form 8-K filed December 3, 2012).
10.5*	Non-Competition, Non-Solicitation and Confidentiality Agreement dated effective December 1, 2012, by and between the Company and Kathleen Skarvan (incorporated by reference to the Company's current report on Form 8-K filed December 3, 2012).
31.1	Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101	Financial statements from the quarterly report on Form 10-Q of the Company for the quarter ended December 31, 2012, formatted in XBRL: (i) the Condensed Consolidated Balance Sheets, (ii) the Condensed Consolidated Statements of Income, (iii) the Condensed Consolidated Statements of Cash Flows, and (iv) the Notes to Condensed Consolidated Financial Statements.

\* Management compensatory plan or agreement.

## WAIVER AGREEMENT

This **WAIVER AGREEMENT** (this "Agreement"), made and entered into as of November 13, 2012, is by and between Electromed, Inc., a Minnesota corporation (the "Borrower"), and U.S. Bank National Association, a national banking association (the "Bank").

### RECITALS

A. The Bank and the Borrower entered into that certain Amended and Restated Credit Agreement dated as of November 7, 2011, between the Bank and the Borrower, as amended by that certain First Amendment to Credit Agreement dated as of December 30, 2011, that certain Consent and Waiver and Second Amendment to Credit Agreement dated as of May 14, 2012, and that certain Waiver and Third Amendment to Credit Agreement dated as of September 28, 2012 (as further amended, restated or otherwise modified from time to time, the "Credit Agreement").

B. Section 6.15 of the Credit Agreement forbids the Borrower from permitting the Fixed Charge Coverage Ratio as of the last day of any fiscal quarter for the four consecutive fiscal quarters ending on that date to be less than 1.2 to 1.0. The Borrower has informed the Bank that the Fixed Charge Coverage Ratio for the fiscal quarter ending September 30, 2012, is less than 1.2 to 1.0, which constitutes an Event of Default under Section 7.1(c) of the Credit Agreement (the "FCCR Event of Default").

C. Section 6.16 of the Credit Agreement forbids the Borrower from permitting the Total Cash Flow Leverage Ratio as of the last day of any fiscal quarter for the four consecutive fiscal quarters ending on that date to be more than 3.5 to 1.0. The Borrower has informed the Bank that the Total Cash Flow Leverage Ratio for the fiscal quarter ending September 30, 2012, is more than 3.5 to 1.0, which constitutes an Event of Default under Section 7.1(c) of the Credit Agreement (the "TCFL Event of Default" and together with the FCCR Event of Default, collectively, the "Existing Defaults").

The Bank has agreed to waive the Existing Defaults, subject to the terms and conditions set forth in this Agreement.

### AGREEMENT

**NOW, THEREFORE**, for good and valuable consideration, the receipt and adequacy of which are hereby acknowledged, the parties hereto hereby covenant and agree to be bound as follows:

**Section 1. Capitalized Terms.** Capitalized terms used and not otherwise defined herein shall have the meanings assigned to them in the Credit Agreement, unless the context otherwise requires.

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**Section 2. Waiver.**

**2.1. Waiver.** Upon the effectiveness of this Agreement pursuant to Section 3 hereof, the Bank hereby waives the Existing Defaults.

**2.2. Scope of Waiver.** The waiver set forth in Section 2.1 hereof is limited to the express terms thereof, and nothing herein shall be deemed a consent or waiver by the Bank with respect to any other term, condition, representation, or covenant applicable to the Borrower under the Credit Agreement or any of the other agreements, documents, or instruments executed and delivered in connection therewith, or of the covenants described therein. The waiver set forth herein shall not be deemed to be a course of action upon which the Borrower or its Subsidiaries may rely in the future.

**Section 3. Effectiveness of Waiver.** The waiver set forth in Section 2.1 hereof shall become effective upon the delivery of, or compliance with, the following:

**3.1.** This Agreement, duly executed by the Borrower and delivered (including by way of telecopy or other electronic transmission (including by e-mail in .pdf format), in each case with original signatures to follow promptly thereafter) to the Bank.

**3.2.** The Borrower shall have satisfied such other conditions as specified by the Bank, including payment of all unpaid legal fees and expenses incurred by the Bank through the date of this Agreement in connection with the Credit Agreement and this Agreement and requested to be paid by the Bank.

**Section 4. Release, No Waiver, Representations, Warranties, Authority, No Adverse Claim.**

**4.1. Release of Claims.** The Borrower, for itself and on behalf of its legal representatives, successors, and assigns, hereby (a) expressly waives, releases, and relinquishes the Bank from any and all claims, offsets, defenses, affirmative defenses, and counterclaims of any kind or nature whatsoever that the Borrower has asserted, or might assert, against the Bank with respect to the Obligations, the Credit Agreement (including as affected by this Agreement), and any other Loan Document, in each case arising on or before the date hereof, such waiver and release being with full knowledge and understanding of the circumstances and effect thereof, and (b) expressly covenants and agrees never to institute, cause to be instituted, or continue prosecution of any suit or other form of action or proceeding of any kind or nature whatsoever against the Bank by reason of or in connection with any of the foregoing matters, claims, or causes of action.

**4.2. No Waiver.** The execution of this Agreement and acceptance of any documents related hereto shall not be deemed to be a waiver of any Default or Event of Default under the Credit Agreement (other than as specifically set forth in Section 2 of this Agreement) or breach, default, or event of default under any Security Document or other document held by the Bank, whether or not known to the Bank and whether or not existing on the date of this Agreement.

**4.3. Reassertion of Representations and Warranties, No Default.** The Borrower hereby represents that on and as of the date hereof and after giving effect to this Agreement (a) all of the representations and warranties in the Credit Agreement and the Security Documents are true, correct, and complete in all material respects, without duplication as to any materiality modifiers, qualifications, or limitations set forth in Article IV of the Credit Agreement, in each case as of the date hereof as though made on and as of such date, except (i) for changes permitted by the terms of the Credit Agreement and (ii) to the extent that any such representations and warranties expressly relate to an earlier date, in which case such representations and warranties were true and correct in all material respects as of such earlier date, and (b) there will exist no Default or Event of Default under the Loan Documents as affected by this Agreement on such date that the Bank has not expressly waived in writing.

**4.4. Authority, No Conflict, No Consent Required.** The Borrower represents and warrants that it has the power, legal right, and authority to enter into the Agreement and has duly authorized as appropriate the execution and delivery of the Agreement by proper corporate action, and neither the Agreement nor the agreements herein contravene or constitute a default under any agreement, instrument, or indenture to which the Borrower is a party or a signatory, any provision of the Borrower's articles of incorporation or bylaws, or any other agreement or requirement of law, or result in the imposition of any Lien on any of its property under any agreement binding on or applicable to the Borrower or any of its property except, if any, in favor of the Bank. The Borrower represents and warrants that no consent, approval, or authorization of or registration or declaration with any Person, including but not limited to any governmental authority, is required in connection with the execution and delivery of the Agreement or the performance of obligations of the Borrower therein described, except for those that the Borrower has obtained or provided and as to which the Borrower has delivered certified copies of documents evidencing each such action to the Bank.

**4.5. No Adverse Claim.** The Borrower warrants, acknowledges, and agrees that no events have taken place and no circumstances exist at the date hereof that would give the Borrower a basis to assert a defense, offset, or counterclaim to any claim of the Bank with respect to the Obligations.

**Section 5. Affirmation of Loan Documents, Further References, Affirmation of Security Interest.** Each of the Bank and the Borrower acknowledge and affirm that the Credit Agreement, the Security Documents, and each of the other Loan Documents to which it is a party is hereby ratified and confirmed in all respects and all terms, conditions, and provisions of each such Loan Document shall remain unmodified and in full force and effect. The Borrower confirms to the Bank that the Obligations are and continue to be secured by the security interest granted in favor of the Bank under the Security Documents and that all of the terms, conditions, provisions, agreements, requirements, promises, obligations, duties, covenants, and representations of the Borrower under such documents and any and all other documents and agreements entered into with respect to the obligations under the Credit Agreement are hereby ratified, assumed, and affirmed in all respects by the Borrower.

**Section 6. Merger and Integration, Superseding Effect.** This Agreement, on and after the date hereof, embodies the entire agreement and understanding between the parties hereto and supersedes and has merged into this Agreement all prior oral and written agreements on the same subjects by and between the parties hereto with the effect that this Agreement shall control with respect to the specific subjects hereof and thereof.

**Section 7. Severability.** Whenever possible, each provision of this Agreement and any other statement, instrument, or transaction contemplated hereby or relating hereto shall be interpreted so as to be effective, valid, and enforceable under the applicable law of any jurisdiction, but if any provision of this Agreement or any other statement, instrument, or transaction contemplated hereby or relating hereto is held to be prohibited, invalid, or unenforceable under the applicable law, such provision shall be ineffective in such jurisdiction only to the extent of such prohibition, invalidity, or unenforceability, without invalidating or rendering unenforceable the remainder of such provision or the remaining provisions of this Agreement or any other statement, instrument, or transaction contemplated hereby or relating hereto in such jurisdiction, or affecting the effectiveness, validity, or enforceability of such provision in any other jurisdiction.

**Section 8. Successors.** This Agreement shall be binding upon the Borrower, the Bank, and their respective successors and assigns, and shall inure to the benefit of the Borrower, the Bank, and the successors and assigns of the Bank.

**Section 9. Expenses.** The Borrower shall pay the Bank, upon execution of this Agreement, the fees and expenses as provided in Section 8.2 of the Credit Agreement.

**Section 10. Headings.** The headings of various sections of this Agreement are for reference only and shall not be deemed to be a part of this Agreement.

**Section 11. Counterparts.** This Agreement may be executed in several counterparts as deemed necessary or convenient, each of which, when so executed, shall be deemed an original, provided that all such counterparts shall be regarded as one and the same document.

**Section 12. Governing Law. THE VALIDITY, CONSTRUCTION AND ENFORCEABILITY OF THIS AGREEMENT SHALL BE GOVERNED BY THE INTERNAL LAWS OF THE STATE OF MINNESOTA, WITHOUT GIVING EFFECT TO CONFLICT OF LAWS PRINCIPLES THEREOF, BUT GIVING EFFECT TO FEDERAL LAWS OF THE UNITED STATES APPLICABLE TO NATIONAL BANKS.**

[The remainder of this page is intentionally left blank]



IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed as of the date and year first above written.

**BORROWER:**

ELECTROMED, INC.

By: /s/ Jeremy T. Brock

Name: Jeremy T. Brock

Title: Chief Financial Officer

**BANK:**

U.S. BANK NATIONAL ASSOCIATION

By: /s/ Daniel J. Miller

Name: Daniel J. Miller

Title: Vice President

Signature Page to Waiver

**AMENDED AND RESTATED EMPLOYMENT AGREEMENT**

This Amended and Restated Employment Agreement (“Amended Agreement”) is effective as of November 15, 2012 (the “Effective Date”), by and among Electromed, Inc., a Minnesota corporation (the “Corporation”), and Jeremy Brock (“Employee”).

**RECITALS**

- A. Employee is currently employed by the Corporation as its Chief Financial Officer, and the Corporation and the Employee are parties to an Employment Agreement, dated as of October 18, 2011 (the “Original Agreement”).
- B. The Corporation wishes to continue to employ Employee to the position of Chief Financial Officer and Employee wishes to continue his employment pursuant to the terms and conditions set forth in this Amended Agreement.
- C. The Corporation and Employee desire to enter into this Amended Agreement, and it is the intention of the Corporation and Employee that this Amended Agreement entirely supersedes any prior agreements with respect hereto.

**AGREEMENT**

In consideration of the above recitals and the mutual promises set forth in this Amended Agreement, the parties agree as follows:

1. Nature and Capacity of Employment. Effective as of the Effective Date, the Corporation hereby agrees to continue to employ the Employee as its Chief Financial Officer, subject to the direction of the Board of Directors of the Corporation and pursuant to the terms and conditions set forth in this Amended Agreement. The Employee hereby agrees to continue acting in that capacity under the terms and conditions set forth in this Amended Agreement. The Employee agrees to perform or be available to perform the functions of this position, pursuant to the terms of this Amended Agreement.

2. Term of Employment. The term of the Employee’s employment hereunder shall commence on the Effective Date of this Amended Agreement and shall continue thereafter through the last day of fiscal year 2014 (“Initial Term”), unless terminated earlier in accordance with Paragraph 4 of this Amended Agreement. The term of this Amended Agreement and the Employee’s employment hereunder shall automatically renew for successive one year periods beyond the expiration of the Initial Term (the “Renewal Term”), unless at least ninety (90) days prior to the expiration of the Initial Term or any Renewal Term either party hereto gives written notice to the other party that it does not intend to renew this Amended Agreement for the coming year. During the Initial Term or any Renewal Term, this Amended Agreement may be terminated pursuant to the terms of Paragraph 4 of this Amended Agreement.

3. Compensation and Benefits.

3.1. Base Salary. As of the Effective Date, the Corporation agrees to pay the Employee an annualized base salary of \$145,000.00, which amount shall be earned by the Employee on a pro rata basis as the Employee performs services and which shall be paid according to the Corporation's normal payroll practices. The Board of Directors acting reasonably shall review and determine the amount of Base Salary payable pursuant to this Paragraph 3.1.

3.2. Non-Equity Incentive Compensation. For the fiscal year ending June 30, 2013, Employee shall receive a bonus in the maximum aggregate amount of 20% of the base salary set forth in Paragraph 3.1 only if he achieves the goals and milestones set forth in the Fiscal 2013 CFO Bonus Plan, as such goals have been determined by, and as achievement against such goals will be evaluated by, the Personnel and Compensation Committee of the Board of Directors. Future Non-Equity Incentive Compensation will be determined by the Personnel and Compensation Committee or the Board of Directors in their discretion.

3.3. Incentive Stock Option. On the second business day following the release of the Corporation's Form 10-Q for the first quarter of its 2013 fiscal year, Employee shall be granted a non-qualified stock option to purchase 20,000 shares of the Corporation's common stock pursuant to the Corporation's 2012 Stock Incentive Plan. The option shall have an exercise price equal to the fair market value of the Corporation's common stock on the date of the grant, shall have a 10-year term, and shall vest as to 6,667 shares on the last day of each of the Corporation's fiscal years ending June 30, 2013, 2014 and 2015 (as to the final 6,666 shares). The remaining terms of the option will be governed by the 2012 Stock Incentive Plan and the non-qualified stock option agreement to be executed by the Corporation and the Employee on or about the date of grant.

3.4. Employee Benefits. During the Employee's employment with the Corporation, the Employee shall be entitled to participate in the retirement plans, health plans, and all other employee benefits made available by the Corporation, and as they may be changed from time to time. The Employee acknowledges and agrees that he will be subject to all eligibility requirements and all other provisions of these benefits plans, and that the Corporation is under no obligation to the Employee to establish and maintain any employee benefit plan in which the Employee may participate. The terms and provisions of any employee benefit plan of the Corporation are matters within the exclusive province of the Corporation's Board of Directors, subject to applicable law.

3.5. Paid Time Off. The Corporation agrees that the Employee shall be entitled to Paid Time Off ("PTO") of up to fifteen (15) days per calendar year, prorated for any partial calendar year of employment, without reduction of the minimum annual base salary payable to the Employee pursuant to Paragraph 3.1 of this Amended Agreement. PTO which is unused at the end of any calendar year will carry over to the next calendar year, subject to the Corporation's limitations on carry-over and accrual maximums. At the end of Employee's employment for any reason, the Corporation will pay Employee for his ending balance of unused PTO.

3.6. Other Benefits: During the Initial Term or Renewal Term, the Corporation shall directly pay the cost of a cell phone or wireless handheld device for the Employee's use. Additionally, during the Initial Term or any Renewal Term, the Corporation shall provide automobile lease payments up to an amount of \$400 per month. The Corporation shall also provide a corporate credit card for approved business expenses and shall otherwise reimburse the Employee for, or pay directly, all reasonable business expenses incurred by the Employee in the performance of his duties under this Amended Agreement, provided that the Employee incurs and accounts for such expenses in accordance with all Corporation policies and directives in effect from time to time.

4. Termination of Employment Prior to the End of the Initial Term or Renewal Term. The Employee's employment may be terminated prior to the expiration of the Term or a Renewal Term as follows:

4.1. For Cause Termination, Without Severance. Notwithstanding anything contained herein to the contrary, the Corporation may discharge the Employee for Cause and terminate this Amended Agreement immediately upon written notice to the Employee. For the purposes of this Amended Agreement, "Cause" shall mean the occurrence of any of the following:

- (i) Employee's material failure to perform his job duties competently as reasonably determined by the Corporation's Board of Directors; or
- (ii) gross misconduct by the Employee which the Corporation's Board of Directors determines is (or will be if continued) demonstrably and materially damaging to the Corporation; or
- (iii) fraud, misappropriation, or embezzlement by the Employee; or
- (iv) conviction of a felony crime or a crime of moral turpitude; or
- (v) conduct in the course of employment that the Corporation's Board of Directors determines is unethical; or
- (vii) the material breach of this Amended Agreement by the Employee.

If the Corporation terminates the Employee's employment for Cause pursuant to this Paragraph 4.1, the Employee shall not be entitled to severance pay.

4.2. Without Cause, With Severance. The Corporation may terminate the Employee's employment immediately at any time and for any reason without Cause upon providing notice to the Employee. However, in such event, provided that the Employee meets all of the conditions set forth in this paragraph for receiving severance pay, the Corporation shall pay the Employee severance pay in the amount of one year's base salary at his then current base salary (the "Severance Amount") payable in a lump sum within sixty (60) days after termination. The Employee shall only be entitled to receive the Severance Amount described herein if the Employee (a) complies with his separate Non-Competition, Non-Solicitation, and Confidentiality Agreement with an effective date of October 18, 2011 and (b) signs, does not rescind, and complies with a Confidential Separation Agreement at the time of termination in a form prepared by the Corporation that includes in part: (i) agreement to a general release of any and all legal claims; (ii) return of all of the Corporation's property in the Employee's possession; and (iii) agreement not to disparage the Corporation and its representatives.

4.3. Resignation by the Employee Due to Change of Control, With Severance. For purposes of this Amended Agreement, "Change of Control" means:

- i. A "change in ownership," as described in Section 1.409A-3(i)(5)(v) of the Treasury Regulations.
- ii. A "change in effective control," as described in Section 1.409A-3(i)(5)(vi) of the Treasury Regulations.
- iii. A "change in ownership of a substantial portion of the assets," as described in Section 1.409A-3(i)(5)(vii) of the Treasury Regulations.

Employee shall have the right to terminate the Employee's employment for any reason within six (6) months following a Change of Control in the Corporation upon providing thirty (30) days advance written notice to the Corporation. The Corporation may then elect either (a) to have the Employee continue performing work for the Corporation throughout the 30 day notice period; or (b) to accept the Employee's resignation effective immediately.

In the event of the Employee's termination of employment with the Corporation following a Change of Control under this Paragraph 4.3, provided that the Employee meets all of the conditions set forth in this paragraph for receiving severance pay, the Corporation shall pay the Employee the Severance Amount outlined in Paragraph 4.2 above in a lump sum within sixty (60) days after termination. The Employee shall only be entitled to receive the Severance Amount described herein if the Employee (a) complies with his separate Non-Competition, Non-Solicitation, and Confidentiality Agreement with an effective date of October 18, 2011 and (b) signs, does not rescind, and complies with a Confidential Separation Agreement at the time of termination in a form prepared by the Corporation that includes in part: (i) agreement to a general release of any and all legal claims; (ii) return of all of the Corporation's property in the Employee's possession; and (iii) agreement not to disparage the Corporation and its representatives.

4.4. Other Resignation by the Employee, Without Severance. The Employee may resign the Employee's position upon providing sixty (60) days advance, written notice to the Corporation. The Corporation may then elect either (a) to have the Employee continue performing work for the Corporation throughout the 60 day notice period; or (b) to accept the Employee's resignation effective immediately. In the event of the Employee's termination of employment with the Corporation under this Paragraph 4.4, the Employee shall not be paid any severance pay.

4.5. Because of Death, Disability or Incapacity of the Employee, Without Severance. In the event of the Employee's death, this Amended Agreement shall terminate immediately. If the Employee is unable to perform the Employee's essential job functions, with or without reasonable accommodation, for more than ninety (90) days, or such longer period as required by law, in any consecutive twelve (12) month period by reason of physical or mental disability or incapacity, the Corporation may terminate the Employee's employment upon thirty (30) days advance written notice to the Employee. This Paragraph does not relieve the Corporation of any duty to reasonably accommodate a qualifying disability under the Americans with Disabilities Act, the Minnesota Human Rights Act, any legal duty under the Family Medical Leave Act, or any of its other duties pursuant to applicable law. If the Employee's employment is terminated pursuant to this Paragraph, the Employee shall not be entitled to severance pay.

4.6. Non-Renewal By Either Party Upon Expiration of the Initial or Renewal Term. For the avoidance of doubt, the parties agree that either party may elect, with or without cause, not to renew this Amended Agreement at the end of the then-current Term and that Employee shall not be entitled to severance pay in the event of non-renewal by either party.

4.7. Section 409A and Taxes Generally. The Corporation shall be entitled to withhold on and report the making of such payments as may be required by law as determined in the reasonable discretion of the Corporation. Notwithstanding anything in this Agreement to the contrary, if at the time of Employee's separation from service within the meaning of Section 409A of the Internal Revenue Code, Corporation determines that Employee is a "specified employee" within the meaning of Section 409A(a)(2)(B)(i) of the Code, then to the extent any payment or benefit that Employee becomes entitled to under this agreement on account of Employees' separation from service would be considered deferred compensation subject to the twenty percent (20%) additional tax imposed pursuant to Section 409(A)(a) of the Code as a result of the application of Section 409A(a)(2)(B)(i) of the Code, such payment shall not be payable and such benefit shall not be provided until the date that is the earlier of (a) six months and one day after Employee's separation from service and (b) Employee's death. The parties intend that this Agreement will be administered in accordance with Section 409A of the Code and to the extent that any provision of this Agreement is ambiguous as to its compliance with Section 409A of the Code, the provision shall be read in such a manner so that all payments hereunder comply with, or are exempt from, Section 409A of the Code. The parties agree that this Agreement may be amended, as may be necessary to fully comply with, or to be exempt from, Section 409A of the Code and all related rules and regulations in order to preserve the payments and benefits provided hereunder without additional cost to either party.

5. Miscellaneous.

5.1. Integration. This Amended Agreement embodies the entire agreement and understanding among the parties relative to subject matter hereof and supersedes all prior agreements and understandings relating to such subject matter, including but not limited to any earlier employment agreements of or offer letters to the Employee. Notwithstanding the foregoing, this Amended Agreement does not replace or otherwise impact the enforceability of the separate Non-Competition, Non-Solicitation, and Confidentiality Agreement with an effective date of October 18, 2011.

5.2. Applicable Law. This Amended Agreement and the rights of the parties shall be governed by and construed and enforced in accordance with the laws of the state of Minnesota.

5.3. Payments. All amounts paid under this Amended Agreement shall be subject to normal withholdings or such other treatment as required by law.

5.4. Employee's Representations. The Employee represents that he is not subject to any agreement or obligation that would prevent or limit him from entering into this Amended Agreement or that would be breached upon performance of his duties under this Amended Agreement, including but not limited to any duties owed to any former employers not to compete. If the Employee possesses any information that he knows or should know is considered by any third party, such as a former employer of the Employee's, to be confidential, trade secret, or otherwise proprietary, the Employee shall not disclose such information to the Corporation or use such information to benefit the Corporation in any way.

5.5. Counterparts. This Amended Agreement may be executed in several counterparts and as so executed shall constitute one agreement binding on the parties hereto.

5.6. Binding Effect. Except as herein or otherwise provided to the contrary, this Amended Agreement shall be binding upon and inure to the benefit of the Corporation and its successors, assigns and personal representatives without any requirement of the consent of the Employee for assignment of its rights or obligations hereunder.

5.7. Modification. This Amended Agreement shall not be modified or amended except by a written instrument signed by the parties.

5.8. Severability. The invalidity or partial invalidity of any portion of this Amended Agreement shall not invalidate the remainder thereof, and said remainder shall remain in fully force and effect.

5.9. Opportunity to Obtain Advice of Counsel. The Employee acknowledges that the Employee has been advised by the Corporation to obtain legal advice prior to executing this Amended Agreement, and that the Employee had sufficient opportunity to do so prior to signing this Amended Agreement.

**\*\*\*\*remainder of page intentionally left blank—signature page to follow\*\*\*\***

**THIS AMENDED AGREEMENT** was voluntarily and knowingly executed by the parties effective as of the date and year first set forth above.

Date: November 15, 2012

**ELECTROMED, INC.**

/s/ Dr. James Cassidy  
By: Dr. James Cassidy  
Its: Interim Chief Executive Officer

Date: 11/15/2012

**EMPLOYEE:**

/s/ Jeremy Brock  
Jeremy Brock



**WAIVER AND FOURTH AMENDMENT TO CREDIT AGREEMENT**

This **WAIVER AND FOURTH AMENDMENT TO CREDIT AGREEMENT** (this "Amendment"), made and entered into as of February 13, 2013, is by and between Electromed, Inc., a Minnesota corporation (the "Borrower"), and U.S. Bank National Association, a national banking association (the "Bank").

**RECITALS**

A. The Bank and the Borrower entered into that certain Amended and Restated Credit Agreement dated as of November 7, 2011, between the Bank and the Borrower, as amended by that certain First Amendment to Credit Agreement dated as of December 30, 2011, that certain Consent and Waiver and Second Amendment to Credit Agreement dated as of May 14, 2012, and that certain Waiver and Third Amendment to Credit Agreement dated as of September 28, 2012 (as further amended, restated or otherwise modified from time to time, the "Credit Agreement").

B. Section 6.15 of the Credit Agreement forbids the Borrower from permitting the Fixed Charge Coverage Ratio as of the last day of any fiscal quarter for the four consecutive fiscal quarters ending on that date to be less than 1.2 to 1.0. The Borrower has informed the Bank that the Fixed Charge Coverage Ratio for the fiscal quarter ending December 31, 2012, is less than 1.2 to 1.0, which constitutes an Event of Default under Section 7.1(c) of the Credit Agreement (the "FCCR Event of Default").

C. Section 6.16 of the Credit Agreement forbids the Borrower from permitting the Total Cash Flow Leverage Ratio as of the last day of any fiscal quarter for the four consecutive fiscal quarters ending on that date to be more than 3.5 to 1.0. The Borrower has informed the Bank that the Total Cash Flow Leverage Ratio for the fiscal quarter ending December 31, 2012, is more than 3.5 to 1.0, which constitutes an Event of Default under Section 7.1(c) of the Credit Agreement (the "TCFL Event of Default").

D. Section 6.20 of the Credit Agreement provides that in no event shall James J. Cassidy cease to be chief executive officer. The Borrower has informed the Bank that James J. Cassidy is no longer chief executive officer of the Borrower, which constitutes an Event of Default under Section 7.1(c) of the Credit Agreement (the "CEO Event of Default" and together with the FCCR Event of Default and the TCFL Event of Default, the "Existing Defaults").

**AGREEMENT**

**NOW, THEREFORE**, for good and valuable consideration, the receipt and adequacy of which are hereby acknowledged, the parties hereto hereby covenant and agree to be bound as follows:

**Section 1. Capitalized Terms.** Capitalized terms used and not otherwise defined herein shall have the meanings assigned to them in the Credit Agreement, unless the context otherwise requires.

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**Section 2. Waiver.**

**2.1. Waiver.** Upon the effectiveness of this Amendment pursuant to Section 4 hereof, the Bank hereby waives the Existing Defaults.

**2.2. Scope of Waiver.** The waiver set forth in Section 2.1 hereof is limited to the express terms thereof, and nothing herein shall be deemed a consent or waiver by the Bank with respect to any other term, condition, representation, or covenant applicable to the Borrower under the Credit Agreement or any of the other agreements, documents, or instruments executed and delivered in connection therewith, or of the covenants described therein. The waiver set forth herein shall not be deemed to be a course of action upon which the Borrower or its Subsidiaries may rely in the future.

**Section 3. Amendments to Credit Agreement.**

**3.1. Definitions.** The definitions of “Applicable Margin” and “Revolving Commitment Amount” set forth in Section 1.1 of the Credit Agreement are amended and restated to read in their entireties as follows:

“Applicable Margin”: 3.50%.

“Fixed Charge Coverage Ratio”: For the fiscal quarter ending on the date of determination, the ratio of

(a) EBITDA, plus operating lease expense, minus the sum of (i) any Restricted Payments, (ii) 50% of depreciation, and (iii) Cash Taxes,  
to

(b) the sum of cash interest payments and all required principal payments with respect to Total Liabilities (including but not limited to all payments with respect to Capitalized Lease Obligations of the Borrower), plus operating lease expense,

in each case determined for said period in accordance with GAAP.

“Revolving Commitment Amount”: \$2,500,000.

**3.2. Financial Reporting.** Section 5.1(b) of the Credit Agreement is amended to read in its entirety as follows:

(b) As soon as available and in any event within 30 days after the end of each calendar month, (i) unaudited statements of income, cash flow and changes in stockholders’ equity for the Borrower for such month and for the period from the beginning of such fiscal year to the end of such month, and a balance sheet of the Borrower as at the end of such month, setting forth in comparative form figures for the corresponding period for the preceding fiscal year, accompanied by a certificate signed by the chief financial officer of the Borrower stating that such financial statements present fairly the financial condition of the Borrower and that the same have been prepared in accordance with GAAP (except for the absence of footnotes and subject to year end audit adjustments as to the interim statements); (ii) a summary of referrals in form and substance satisfactory to the Bank; and (iii) a summary of product shipments in form and substance satisfactory to the Bank.

3.3. **Permitted Indebtedness.** Section 6.12(d) of the Credit Agreement is amended to read in its entirety as follows:

(d) Intentionally Omitted.

3.4. **Fixed Charge Coverage Ratio.** Section 6.15 of the Credit Agreement is amended to read in its entirety as follows:

Section 6.15 Fixed Charge Coverage Ratio. The Borrower will not permit the Fixed Charge Coverage Ratio, as of the quarter ending September 30, 2013, to be less than 1.15 to 1, for the quarter ending on such date.

3.5. **Minimum EBITDA.** Section 6.16 of the Credit Agreement is amended to read in its entirety as follows:

Section 6.16 Minimum EBITDA. The Borrower will not permit EBITDA, (i) as of the quarter ending March 31, 2013, to be less than negative \$275,000, and (ii) as of the quarter ending June 30, 2013, to be less than \$425,000, in each case for the quarter ending on such date.

3.6. **Key Man Life Insurance.** Section 6.18 of the Credit Agreement is amended to read in its entirety as follows:

Section 6.18. Intentionally Omitted.

3.7. **Form of Compliance Certificate.** Exhibit G to the Credit Agreement is amended to read in its entirety as set forth on Exhibit A hereto.

**Section 4. Effectiveness of Waiver.** The waiver set forth in Section 2.1 hereof and amendments set forth in Section 3 hereof shall become effective upon the delivery of, or compliance with, the following:

4.1. This Amendment, duly executed by the Borrower and delivered (including by way of telecopy or other electronic transmission (including by e-mail in .pdf format), in each case with original signatures to follow promptly thereafter) to the Bank.

4.2. A certificate of an officer of the Borrower certifying to a true and correct copy of resolutions of the Borrower authorizing and ratifying this Amendment, each in form and substance satisfactory to the Bank.

4.3. The Bank shall have received a non-refundable amendment fee in the amount of \$5,000.

4.4. The Borrower shall have satisfied such other conditions as specified by the Bank, including payment of all unpaid legal fees and expenses incurred by the Bank through the date of this Amendment in connection with the Credit Agreement and this Amendment and requested to be paid by the Bank.

**Section 5. Release, No Waiver, Representations, Warranties, Authority, No Adverse Claim.**

5.1. **Release of Claims.** The Borrower, for itself and on behalf of its legal representatives, successors, and assigns, hereby (a) expressly waives, releases, and relinquishes the Bank from any and all claims, offsets, defenses, affirmative defenses, and counterclaims of any kind or nature whatsoever that the Borrower has asserted, or might assert, against the Bank with respect to the Obligations, the Credit Agreement (including as affected by this Amendment), and any other Loan Document, in each case arising on or before the date hereof, such waiver and release being with full knowledge and understanding of the circumstances and effect thereof, and (b) expressly covenants and agrees never to institute, cause to be instituted, or continue prosecution of any suit or other form of action or proceeding of any kind or nature whatsoever against the Bank by reason of or in connection with any of the foregoing matters, claims, or causes of action.

5.2. **No Waiver.** The execution of this Amendment and acceptance of any documents related hereto shall not be deemed to be a waiver of any Default or Event of Default under the Credit Agreement (other than as specifically set forth in Section 2 of this Amendment) or breach, default, or event of default under any Security Document or other document held by the Bank, whether or not known to the Bank and whether or not existing on the date of this Amendment.

5.3. **Reassertion of Representations and Warranties, No Default.** The Borrower hereby represents that on and as of the date hereof and after giving effect to this Amendment (a) all of the representations and warranties in the Credit Agreement and the Security Documents are true, correct, and complete in all material respects, without duplication as to any materiality modifiers, qualifications, or limitations set forth in Article IV of the Credit Agreement, in each case as of the date hereof as though made on and as of such date, except (i) for changes permitted by the terms of the Credit Agreement and (ii) to the extent that any such representations and warranties expressly relate to an earlier date, in which case such representations and warranties were true and correct in all material respects as of such earlier date, and (b) there will exist no Default or Event of Default under the Loan Documents as affected by this Amendment on such date that the Bank has not expressly waived in writing.

5.4. **Authority, No Conflict, No Consent Required.** The Borrower represents and warrants that it has the power, legal right, and authority to enter into the Amendment and has duly authorized as appropriate the execution and delivery of the Amendment by proper corporate action, and neither the Amendment nor the agreements herein contravene or constitute a default under any agreement, instrument, or indenture to which the Borrower is a party or a signatory, any provision of the Borrower's articles of incorporation or bylaws, or any other agreement or requirement of law, or result in the imposition of any Lien on any of its property under any agreement binding on or applicable to the Borrower or any of its property except, if any, in favor of the Bank. The Borrower represents and warrants that no consent, approval, or authorization of or registration or declaration with any Person, including but not limited to any governmental authority, is required in connection with the execution and delivery of the Amendment or the performance of obligations of the Borrower therein described, except for those that the Borrower has obtained or provided and as to which the Borrower has delivered certified copies of documents evidencing each such action to the Bank.

**5.5. No Adverse Claim.** The Borrower warrants, acknowledges, and agrees that no events have taken place and no circumstances exist at the date hereof that would give the Borrower a basis to assert a defense, offset, or counterclaim to any claim of the Bank with respect to the Obligations.

**Section 6. Affirmation of Loan Documents, Further References, Affirmation of Security Interest.** Each of the Bank and the Borrower acknowledge and affirm that the Credit Agreement, the Security Documents, and each of the other Loan Documents to which it is a party is hereby ratified and confirmed in all respects and all terms, conditions, and provisions of each such Loan Document shall remain unmodified and in full force and effect. The Borrower confirms to the Bank that the Obligations are and continue to be secured by the security interest granted in favor of the Bank under the Security Documents and that all of the terms, conditions, provisions, agreements, requirements, promises, obligations, duties, covenants, and representations of the Borrower under such documents and any and all other documents and agreements entered into with respect to the obligations under the Credit Agreement are hereby ratified, assumed, and affirmed in all respects by the Borrower.

**Section 7. Merger and Integration, Superseding Effect.** This Amendment, on and after the date hereof, embodies the entire agreement and understanding between the parties hereto and supersedes and has merged into this Amendment all prior oral and written agreements on the same subjects by and between the parties hereto with the effect that this Amendment shall control with respect to the specific subjects hereof and thereof.

**Section 8. Severability.** Whenever possible, each provision of this Amendment and any other statement, instrument, or transaction contemplated hereby or relating hereto shall be interpreted so as to be effective, valid, and enforceable under the applicable law of any jurisdiction, but if any provision of this Amendment or any other statement, instrument, or transaction contemplated hereby or relating hereto is held to be prohibited, invalid, or unenforceable under the applicable law, such provision shall be ineffective in such jurisdiction only to the extent of such prohibition, invalidity, or unenforceability, without invalidating or rendering unenforceable the remainder of such provision or the remaining provisions of this Amendment or any other statement, instrument, or transaction contemplated hereby or relating hereto in such jurisdiction, or affecting the effectiveness, validity, or enforceability of such provision in any other jurisdiction.

**Section 9. Successors.** This Amendment shall be binding upon the Borrower, the Bank, and their respective successors and assigns, and shall inure to the benefit of the Borrower, the Bank, and the successors and assigns of the Bank.

**Section 10. Expenses.** The Borrower shall pay the Bank, upon execution of this Amendment, the fees and expenses as provided in Section 8.2 of the Credit Agreement.

**Section 11. Headings.** The headings of various sections of this Amendment are for reference only and shall not be deemed to be a part of this Amendment.

**Section 12. Counterparts.** This Amendment may be executed in several counterparts as deemed necessary or convenient, each of which, when so executed, shall be deemed an original, provided that all such counterparts shall be regarded as one and the same document.

**Section 13. Governing Law. THE VALIDITY, CONSTRUCTION AND ENFORCEABILITY OF THIS AMENDMENT SHALL BE GOVERNED BY THE INTERNAL LAWS OF THE STATE OF MINNESOTA, WITHOUT GIVING EFFECT TO CONFLICT OF LAWS PRINCIPLES THEREOF, BUT GIVING EFFECT TO FEDERAL LAWS OF THE UNITED STATES APPLICABLE TO NATIONAL BANKS.**

[The remainder of this page is intentionally left blank]

IN WITNESS WHEREOF, the parties hereto have caused this Amendment to be executed as of the date and year first above written.

**BORROWER:**

ELECTROMED, INC.

By: /s/ Jeremy T. Brock  
Name: Jeremy T. Brock  
Title: Chief Financial Officer

**BANK:**

U.S. BANK NATIONAL ASSOCIATION

By: /s/ Daniel J. Miller  
Name: Daniel J. Miller  
Title: Vice President

Signature Page to Amendment

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FORM OF COMPLIANCE CERTIFICATE

To: U.S. Bank National Association:

THE UNDERSIGNED HEREBY CERTIFIES THAT:

(1) I am the duly elected chief financial officer of Electromed, Inc. (the "Borrower");

(2) I have reviewed the terms of the Amended and Restated Credit Agreement dated as of November 7, 2011, between the Borrower and U.S. Bank National Association (as amended, restated, or otherwise modified from time to time, the "Credit Agreement"), and I have made, or have caused to be made under my supervision, a detailed review of the transactions and conditions of the Borrower during the accounting period covered by the Attachment hereto;

(3) The examination described in paragraph (2) did not disclose, and I have no knowledge, whether arising out of such examinations or otherwise, of the existence of any condition or event that constitutes a Default or an Event of Default (as such terms are defined in the Credit Agreement) during or at the end of the accounting period covered by the Attachment hereto or as of the date of this Certificate, except as described below (or on a separate attachment to this Certificate). The exceptions listing, in detail, the nature of the condition or event, the period during which it has existed, and the action the Borrower has taken, is taking, or proposes to take with respect to each such condition or event are as follows:

\_\_\_\_\_  
\_\_\_\_\_

The foregoing certification, together with the computations in the Attachment hereto and the financial statements delivered with this Certificate in support hereof, are made and delivered this \_\_\_ day of \_\_\_\_\_, \_\_\_\_\_ pursuant to Section 5.1(c) of the Credit Agreement.

ELECTROMED, INC.

By \_\_\_\_\_

Title \_\_\_\_\_

\_\_\_\_\_



ATTACHMENT TO COMPLIANCE CERTIFICATE

This Compliance Certificate is delivered under the Credit Agreement dated as of November 7, 2011 (as amended, restated or other wise modified from time to time, the "Credit Agreement"), between Electromed and U.S. Bank National Association.

All terms used in this Compliance Certificate shall have the meanings given them in the Credit Agreement.

The figures used in this Compliance Certificate were determined as of \_\_\_\_\_.

I certify that the following amounts were correctly determined according to the Credit Agreement as of the date set forth above:

**[1. Minimum EBITDA In Compliance Yes \_\_\_\_\_ No \_\_\_\_\_]**

For the quarters ending March 31, 2013, and June 30, 2013]

*EBITDA*

\_\_\_\_\_

**[1. Fixed Charge Coverage Ratio In Compliance Yes \_\_\_\_\_ No \_\_\_\_\_]**

For the quarter ending September 30, 2013]

*EBITDA*

*For quarter end*

*Plus:*

*Operating lease expense*

\_\_\_\_\_

\_\_\_\_\_

*Less:*

*Cash Taxes*

*Cash Dividends/Cash distributions*

*Maintenance CAPEX (50% of Depreciation Expense)*

\_\_\_\_\_

\_\_\_\_\_

*Total (A)*

*Required Principal Payments*

*Plus Cash Interest Payments*

*Plus Rental or Lease Expense*

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

*Total (B)*

*Ratio of (A) to (B)*

**2. No Additional Interest Bearing Debt (Tested Quarterly)**

**In Compliance Yes \_\_\_\_\_ No \_\_\_\_\_**



I further certify that the Borrower is in compliance with all other terms and conditions of the Agreement and that no Event of Default or event that with notice or lapse of time would be an Event of Default has occurred since the last Compliance Certificate provided to the Bank.

**Electromed, Inc.**

By \_\_\_\_\_

Title \_\_\_\_\_

**Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Kathleen S. Skarvan, certify that:

1. I have reviewed this report on Form 10-Q of Electromed, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations, and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15(d)-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's Board of Directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize, and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 14, 2013

By: /s/ Kathleen S. Skarvan  
Chief Executive Officer

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**Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Jeremy T. Brock, certify that:

1. I have reviewed this report on Form 10-Q of Electromed, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations, and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15(d)-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's Board of Directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize, and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 14, 2013

By: /s/ Jeremy T. Brock  
Chief Financial Officer

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**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with this Periodic Report of Electromed, Inc. (the "Company") on Form 10-Q for the period ended December 31, 2012, as filed with the Securities and Exchange Commission (the "Report"), I, Kathleen S. Skarvan, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: February 14, 2013

/s/ Kathleen S. Skarvan  
Kathleen S. Skarvan  
Chief Executive Officer

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**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with this Periodic Report of Electromed, Inc. (the "Company") on Form 10-Q for the period ended December 31, 2012, as filed with the Securities and Exchange Commission (the "Report"), I, Jeremy T. Brock, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: February 14, 2013

/s/ Jeremy T. Brock  
Jeremy T. Brock  
Chief Financial Officer

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