DYNACQ HEALTHCARE INC
Form 10-Q
January 12, 2010
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended November 30, 2009

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

Commission File Number: 000-21574

DYNACQ HEALTHCARE, INC.

(Exact name of registrant as specified in its charter)

Nevada	**76-0375477**
(State or other jurisdiction of	**(I.R.S. Employer**
incorporation or organization)	**Identification No.)**
10304 Interstate 10 East, Suite 369	
Houston, Texas	**77029**
(Address of principal executive offices)	**(Zip Code)**

(713) 378-2000

(Registrant s telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x 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. (Check One):

Large accelerated filer ¨ Accelerated filer ¨ Non-accelerated filer ¨ Smaller reporting company x

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

As of January 6, 2010, the number of shares outstanding of the registrant s common stock, par value $.001 per share, was 15,219,262.

Table of Contents

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To: The Stockholders and Board of Directors
Dynacq Healthcare, Inc.

Houston, Texas

We have reviewed the accompanying consolidated balance sheet of Dynacq Healthcare, Inc., as of November 30, 2009, and the related consolidated statements of operations and cash flows for the three-month periods ended November 30, 2009 and 2008. These interim financial statements are the responsibility of the Company s management.

We conducted our reviews in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to the accompanying consolidated interim financial statements for them to be in conformity with United States of America generally accepted accounting principles.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of Dynacq Healthcare, Inc., as of August 31, 2009, and the related consolidated statements of operations, stockholders equity, and cash flows for the year then ended not presented herein, and in our report dated November 23, 2009, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying consolidated balance sheet as of August 31, 2009, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ Killman, Murrell & Company, P.C.
Killman, Murrell & Company, P.C.
Houston, Texas
January 12, 2010

Table of Contents

PART I - FINANCIAL INFORMATION

ITEM I - FINANCIAL STATEMENTS

Dynacq Healthcare, Inc.

Consolidated Balance Sheets

	November 30, 2009 (Reviewed)	August 31, 2009 (Audited)
Assets		
Current assets:		
Cash and cash equivalents	$ 35,596,563	$ 39,112,965
Accounts receivable, net of contractual allowances of approximately $244,042,000 and $236,996,000 at November 30, 2009 and August 31, 2009, respectively	8,039,636	8,671,389
Inventories	1,546,899	1,518,815
Interest receivable	481,835	270,374
Prepaid expenses	637,883	373,949
Income tax receivable	959,863	
Deferred tax assets	663,026	770,400
Total current assets	47,925,705	50,717,892
Investments available-for-sale	20,389,016	18,572,169
Property and equipment, net	14,902,032	14,858,207
Income tax receivable	868,249	868,249
Other assets	252,210	250,664
Total assets	$ 84,337,212	$ 85,267,181

See accompanying notes.

Table of Contents

Dynacq Healthcare, Inc.

Consolidated Balance Sheets (continued)

	November 30, 2009 (Reviewed)	August 31, 2009 (Audited)
Liabilities and stockholders equity		
Current liabilities:		
Accounts payable	$ 3,547,693	$ 3,395,053
Accrued liabilities	5,133,354	6,244,978
Notes payable	126,505	251,131
Current portion of capital lease obligations	78,579	80,627
Current taxes payable	83,000	128,420
Total current liabilities	8,969,131	10,100,209
Non-current liabilities:		
Long-term portion of capital lease obligations	317,124	335,582
Deferred tax liabilities	3,344,067	2,751,619
Total liabilities	12,630,322	13,187,410
Commitments and contingencies		
Equity:		
Dynacq stockholders equity:		
Preferred stock, $.01 par value; 5,000,000 shares authorized, none issued or outstanding		
Common stock, $.001 par value; 100,000,000 shares authorized, 15,819,495 and 15,815,120 shares issued at November 30, 2009 and August 31, 2009, respectively	15,819	15,815
Treasury stock, 597,352 and 489,672 shares at November 30, 2009 and August 31, 2009, respectively, at cost	(2,802,792)	(2,429,465)
Additional paid-in capital	14,923,874	14,800,062
Accumulated other comprehensive income	7,493,610	6,297,908
Retained earnings	51,819,105	53,151,206
Total Dynacq stockholders equity	71,449,616	71,835,526
Non-controlling interest	257,274	244,245
Total equity	71,706,890	72,079,771
Total liabilities and equity	$ 84,337,212	$ 85,267,181

See accompanying notes.

Table of Contents

Dynacq Healthcare, Inc.

Consolidated Statements of Operations

(Reviewed)

	Three months ended November 30, 2009	2008
Net patient service revenue	$ 8,984,611	$ 10,879,238
Costs and expenses:		
Compensation and benefits	4,081,907	3,681,540
Medical services and supplies	2,719,503	3,289,820
Other operating expenses	4,683,810	4,635,546
Depreciation and amortization	265,979	394,224
Total costs and expenses	11,751,199	12,001,130
Operating loss	(2,766,588)	(1,121,892)
Other income:		
Rent and other income	349,618	71,678
Interest income	454,895	155,841
Interest expense	(11,393)	(10,997)
Total other income, net	793,120	216,522
Loss before income taxes	(1,973,468)	(905,370)
Benefit for income taxes	621,896	261,464
Net loss	(1,351,572)	(643,906)
Less: Net loss attributable to the noncontrolling interest	19,469	1,354
Net loss attributable to Dynacq Healthcare, Inc.	$ (1,332,103)	$ (642,552)
Basic loss per common share:		
Net loss attributable to Dynacq Healthcare, Inc. stockholders	$ (0.09)	$ (0.04)
Diluted loss per common share:		
Net loss attributable to Dynacq Healthcare, Inc. stockholders	$ (0.09)	$ (0.04)
Weighted average common shares outstanding - basic	15,267,602	15,555,731
Weighted average common shares outstanding - diluted	15,267,602	15,555,731

See accompanying notes.

Table of Contents

Dynacq Healthcare, Inc.

Consolidated Statements of Cash Flows

(Reviewed)

	Three months ended November 30, 2009	2008
Cash flows from operating activities		
Net loss	$ (1,332,103)	$ (642,552)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	265,979	394,224
Deferred income taxes	55,982	9,377
Noncontrolling interest	(19,469)	(1,354)
Charge for stock options to employees	112,879	116,474
Changes in operating assets and liabilities:		
Accounts receivable	632,204	6,969,959
Interest receivable	(211,461)	
Inventories	(27,870)	189,063
Prepaid expenses	(263,933)	(71,633)
Income taxes receivable	(959,863)	(3,190,570)
Other assets	(1,547)	(35,246)
Accounts payable	151,909	(322,431)
Accrued liabilities	(1,112,260)	(1,855,495)
Income taxes payable	(45,420)	(4,223,215)
Net cash used in operating activities	(2,754,973)	(2,663,399)
Cash flows from investing activities		
Purchase of equipment	(309,230)	(59,787)
Investment in available-for-sale securities		(3,906,000)
Net cash used in investing activities	(309,230)	(3,965,787)
Cash flows from financing activities		
Principal payments on notes payable	(124,626)	(117,386)
Contributions from, and distributions to noncontrolling interest, net	32,500	
Payments on capital lease	(20,379)	(5,070)
Treasury stock purchase	(373,327)	
Proceeds from exercise of stock options	10,937	
Net cash used in financing activities	(474,895)	(122,456)
Effect of exchange rate changes on cash	22,696	23,158
Net decrease in cash and cash equivalents	(3,516,402)	(6,728,484)
Cash at beginning of period	39,112,965	45,099,800
Cash at end of period	$ 35,596,563	$ 38,371,316
Supplemental cash flow disclosures		
Cash paid during the period for:		

Interest	$ 11,393	$ 9,959
Income taxes	$ 327,405	$ 7,142,944
Non cash investing and financing activities:		
Increase (decrease) in value of investment in bonds	$ 1,816,847	$ (278,000)
Accumulated other comprehensive income	(1,173,006)	278,000
Deferred tax liabilities	(643,841)	
Equipment from capital lease		(435,498)
Capital lease obligation		435,498

See accompanying notes.

7

Table of Contents

Dynacq Healthcare, Inc.

Notes to Consolidated Financial Statements

November 30, 2009

(reviewed)

Basis of Presentation

The accompanying reviewed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete consolidated financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included. All such adjustments are of a normal and recurring nature. The majority of the Company s expenses are cost of revenue items. Costs that could be classified as general and administrative by the Company would include the corporate office costs, including advertising and marketing expenses, which were approximately $1.3 million and $0.9 million for the quarters ended November 30, 2009 and 2008, respectively. These reviewed financial statements should be read in conjunction with the audited financial statements at August 31, 2009. Operating results for the quarter ended November 30, 2009 are not necessarily indicative of the results that may be expected for the year ending August 31, 2010.

Certain previously reported financial information has been reclassified to conform to the current year period s presentation. The impact of such reclassification was not significant to the prior year period s overall presentation.

Cash and Cash Equivalents

The Company considers all highly liquid investments with maturities of three months or less on the date of purchase to be cash equivalents. Cash equivalents are carried at cost, which approximates fair value.

Investments Available-for-Sale

The Company has invested in various bonds. These investments are classified as available-for-sale securities, and are carried at fair value as of November 30, 2009, based on the quoted market prices as of that date. These investments are subject to default risk. The Company intends to hold these for a minimum period of an additional 12 months. Unrealized gains in the fair value are reported in accumulated other comprehensive income, net of related income tax effect. The Company monitors its investment portfolio for any decline in fair value that is other than temporary and records any such impairment as an impairment loss.

Inventories

Inventories, consisting primarily of medical supplies, are stated at the lower of cost or market, with cost determined by use of the average cost method.

General

As of November 30, 2009, the Company operated one facility each in the Houston metropolitan area (Pasadena facility) and in the Dallas-Fort Worth area (Garland facility) and owned 100% of the equity interest in Dynacq Huai Bei Healthcare, Inc. (Dynacq-Huai Bei), a corporation formed under the laws of the People s Republic of China to provide healthcare management services in that country. Effective March 1, 2009, Dynacq-Huai Bei began managing Second People s Hospital in Rui An, China.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. The most significant of the Company s estimates is the determination of revenue to recognize for the services the Company provides and the determination of the

8

Table of Contents

contractual allowance. See Revenue Recognition below for further discussion. Actual results could differ materially from those estimates used in the preparation of these financial statements.

Subsequent Events

The Company has evaluated subsequent events that have occurred through January 12, 2010, which is the date of issuance of these financial statements, and has accounted for and disclosed material subsequent events in these condensed consolidated financial statements as appropriate.

Net Income (Loss) per Share

The following is a reconciliation of the weighted average number of common shares outstanding with the number of shares used in the computations of net income (loss) per common and common equivalent share:

	Three months ended November 30,	
	2009	**2008**
Number of weighted average common shares outstanding	15,267,602	15,555,731
Assumed exercise of stock options		
Average diluted shares outstanding	15,267,602	15,555,731

Basic net income (loss) per share is computed by dividing net income available to common shareholders by the weighted average number of common shares outstanding for the reporting period. Diluted net income (loss) per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. For the calculation of diluted net income (loss) per share, the basic weighted average number of shares is increased by the dilutive effect of stock options determined using the treasury stock method. However, if it is anti-dilutive, the dilutive effect of the stock options is not included in the calculation of diluted net income (loss) per share. Stock options with exercise prices exceeding current market prices that were excluded from the computation of net income (loss) per share amounted to approximately 574,000 shares and 630,000 shares for the quarters ended November 30, 2009 and 2008, respectively.

Stock Based Compensation

The Company s 2000 Incentive Plan (the Plan) provides for options and other stock-based awards that may be granted to eligible employees, officers, consultants and non-employee directors of the Company or its subsidiaries. The Company had reserved 5,000,000 shares of common stock for future issuance under the Plan. As of November 30, 2009, there remain 1,410,404 shares which can be issued under the Plan, after giving effect to stock splits and shares issued under the Plan. The Plan permits stock awards, stock appreciation rights, performance units, and other stock-based awards, all of which may or may not be subject to the achievement of one or more performance objectives.

The purposes of the Plan generally are to retain and attract persons of training, experience and ability to serve as employees of the Company and its subsidiaries and to serve as non-employee directors of the Company, to encourage the sense of proprietorship of such persons and to stimulate the active interest of such persons in the development and financial success of the Company and its subsidiaries.

The Plan is administered by the Compensation Committee of the Board of Directors (the Committee). The Committee has the power to determine which eligible employees will receive awards, the timing and manner of the grant of such awards, the exercise price of stock options (which may not be less than market value on the date of grant), the number of shares, and all of the terms of the awards. The Company may at any time amend or terminate the Plan. However, no amendment that would impair the rights of any participant with respect to outstanding grants can be made without the participant s prior consent. Stockholder approval of an amendment to the Plan is necessary only when required by applicable law or stock exchange rules.

For the quarter ended November 30, 2009, there were no equity-based compensation awards granted. Generally, options granted become exercisable in annual installments of 25 percent beginning on the first

Table of Contents

anniversary date, and expire after five to ten years. The following table summarizes the stock option activities for the quarter ended November 30, 2009 (share amounts in thousands):

	Shares	Weighted Average Option Exercise Price Per Share	Weighted Average Grant Date Fair Value Per Share	Aggregate Intrinsic Value[(1)]
Outstanding, August 31, 2009	1,376	$ 3.47		$ 713,300
Granted				
Exercised	(4)	2.50		
Expired or canceled	(4)	2.50		
Outstanding, November 30, 2009	1,368	$ 3.47		$ 967,969

(1) These amounts represent the difference between the exercise price and $3.75, the closing price of Dynacq common stock on November 30, 2009 as reported on the NASDAQ stock market, for all in-the-money options outstanding. For exercised options, intrinsic value represents the difference between the exercise price and the closing price of Dynacq common stock on the date of exercise.

For the quarter ended November 30, 2009 and 2008, the Company received $10,938 and $-0-, respectively, for stock options exercised.

The following summarizes information related to stock options outstanding at November 30, 2009, and related weighted average price and life information:

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	**Shares**	**Weighted Average Remaining Contractual Life (Years)**	**Weighted Average Exercise Price**	**Shares**	**Weighted Average Exercise Price**
		(Share Amounts In Thousands)			
$ 2.50 2.75	794	3.6	$ 2.53	376	$ 2.53
$ 4.44 5.10	574	3.5	4.78	499	4.73
Total	1,368	3.6	$ 3.47	875	$ 3.78

The above tables for stock option activities and stock options outstanding does not include a performance share award granted on July 25, 2008 by the Compensation Committee to an employee whereby the employee can earn up to 1 million shares of the Company s common stock if certain operating performance criteria are met, beginning in fiscal 2010. The number of shares that are issuable each year is to be determined by quantifying the performance criteria and dividing the quantified amount by $3.74, which was the market price of the Company s stock on the date of grant of the award. The performance period extends for ten years or until such time as the 1 million shares of common stock have been awarded.

Additional information relating to the Plan at November 30, 2009 and August 31, 2009 is as follows (in thousands):

	November 30, 2009	August 31, 2009
Options exercisable	875	881
Options available for grant and reserved common stock shares for stock option plans	1,410	1,407

For the quarter ended November 30, 2009 and 2008, stock-based compensation expense associated with the Company s stock options was $112,879 and $116,474, respectively. The total unrecognized compensation expense

Table of Contents

for outstanding stock options as of November 30, 2009 was $783,000, and will be recognized, in general, over 1.9 years. The weighted average number of years to recognize the compensation expense is 1.0 year.

Fair Value of Financial Instruments

On September 1, 2008, the Company adopted ASC Topic 825-10-25, Financial Instruments (formerly referred to as SFAS No. 159, The Fair Value Option for Financial Assets and Liabilities (SFAS 159)), which permits entities to choose to measure certain financial assets and liabilities at fair value. The adoption of ASC Topic 825-10-25 had no impact on the consolidated financial statements because the Company did not elect the fair value option for any financial assets or financial liabilities that were not already recorded at fair value.

On September 1, 2008, the Company adopted ASC Topic 820, Fair Value Measurements and Disclosures (formerly referred to as SFAS 157) for our financial assets and liabilities. Management uses the fair value hierarchy of ASC Topic 820, which gives the highest priority to quoted prices in active markets. The fair value of financial instruments is estimated based on market trading information, where available. Absent published market values for an instrument or other assets, management uses observable market data to arrive at its estimates of fair value. Management believes that the carrying amount of cash and cash equivalents, accounts receivable and accrued liabilities approximate fair value. ASC Topic 820 defines fair value as an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. As a basis for considering such assumptions, ASC Topic 820 establishes a three-level fair value hierarchy that prioritizes the inputs used to measure fair value. The three levels of inputs used to measure fair value are as follows:

Level 1 Quoted prices in active markets for identical assets or liabilities.

Level 2 Observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets; quoted price for identical or similar assets and liabilities in markets that are not active; or other input that are observable or can be corroborated by observable market data.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. This includes certain pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs.

The following table summarizes our financial assets and liabilities measured and reported in the Company s statement of financial position at fair value on a recurring basis as of November 30, 2009, segregated among the appropriate levels within the fair value hierarchy:

	Fair Value Measurements at November 30, 2009		
	Quoted prices in active markets for identical (Level 1)	**Significant other observable inputs (Level 2)**	**Significant unobservable (Level 3)**
Assets			
Investments available-for-sale		$ 20,389,016	

All of the Company s investments in securities are in perpetual bonds traded on the European markets. The cost of these securities is $9,135,146.

Foreign Currency Translation

The functional currency of the Company as a whole is the U.S. Dollar. The Company has designated the Chinese Yuan Renminbi as the functional currency for its subsidiaries in mainland China, and the U.S. Dollar for Sino Bond Inc. Limited in Hong Kong. Assets and liabilities are translated into U.S. dollars using current exchange rates as of the balance sheet date. Income and expense are translated at average exchange rates prevailing during the period. The effects of foreign currency translation adjustments are included as a component of accumulated other comprehensive income within stockholders equity.

Table of Contents

Revenue Recognition

U.S. Division

Background

The Company s revenue recognition policy is significant because net patient service revenue is a primary component of its results of operations. Revenue is recognized as services are delivered. The determination of the amount of revenue to be recognized in connection with the Company s services is subject to significant judgments and estimates, which are discussed below.

Revenue Recognition Policy

The Company has established billing rates for its medical services which it bills as gross revenue as services are delivered. Gross billed revenues are then reduced by the Company s estimate of the discount (contractual allowance) to arrive at net patient service revenues. Net patient service revenues may not represent amounts ultimately collected. The Company does adjust current period revenue for actual differences in estimated revenue recorded in prior periods and actual cash collections.

Contractual Allowance

Starting March 1, 2008, the Company computes its contractual allowance based on the estimated collections on its gross billed charges. The Company computes its estimate by taking into account collections received, up to 30 days after the end of the period, for the services performed and also estimating amounts collectible within the next six months. Prior to March 1, 2008, the contractual allowance was calculated based on the ratio of the Company s historical cash collections during the trailing twelve months on a case-by-case basis by operating facility. This ratio of cash collections to billed services was then applied to the gross billed services by operating facility. The following table shows gross revenues and contractual allowances for the three months ended November 30, 2009 and 2008:

	2009	2008
Gross billed charges	$ 27,984,386	$ 38,420,463
Contractual allowance	19,599,157	27,541,225
Net revenue	$ 8,385,229	$ 10,879,238
Contractual allowance percentage	70%	72%

A significant amount of our net revenue results from Texas workers compensation claims, which are governed by the rules and regulations of the Texas Department of Workers Compensation (TDWC) and the workers compensation healthcare networks. If one of our hospitals chooses to participate in a network, the amount of revenue that will be generated from workers compensation claims will be governed by the network contract.

For claims arising prior to the implementation of workers compensation networks and out of network claims, inpatient and outpatient surgical services are either reimbursed pursuant to the Acute Care In-Patient Hospital Fee Guideline or at a fair and reasonable rate for services in which the fee guideline is not applicable. Starting March 1, 2008, the Texas Workers Compensation 2008 Acute Care Hospital Outpatient and Inpatient Facility Fee Guidelines (the Guidelines) became effective. Under these Guidelines, the reimbursement amounts are determined by applying the most recently adopted and effective Medicare reimbursement formula and factors; however, if the maximum allowable reimbursement for the procedure performed cannot be calculated using these Guidelines, then reimbursement is determined on a fair and reasonable basis.

Based on these Guidelines, the reimbursement due the Company for workers compensation cases is lower than we previously experienced. The Company has continued accepting Texas workers compensation cases, and has not made any substantial changes in its focus towards such cases. Our net patient service revenue for Texas workers compensation cases as a percentage of gross billings has decreased primarily as a result of lower reimbursement rates for workers compensation procedures still being performed.

12

Table of Contents

Should our facility disagree with the amount of reimbursement provided by a third-party payer, we are required to pursue the MDR process at the TDWC to request proper reimbursement for services. From January 2007 to November 2008, the Company had been successful in its pursuit of collections regarding the stop-loss cases pending before the State Office of Administrative Hearings (SOAH), receiving positive rulings in over 90% of its claims presented for administrative determination. The 2007 district court decision upholding our interpretation of the statute as applied to the stop-loss claims was appealed by certain insurance carriers, and on November 13, 2008 the Third Court of Appeals determined that in order for a hospital to be reimbursed at 75% of its usual and customary audited charges for an inpatient admission, the hospital must not only bill at least $40,000, but also show that the admission involved unusually costly and unusually extensive services. Procedurally, the decision means that each case where a carrier raised an issue regarding whether the services provided were unusually costly or unusually extensive would be remanded to either SOAH or MDR for a case-by-case determination of whether the services provided meet these standards, once the definitions of those standards are determined. As a result of the Third Court of Appeals opinion, any stop-loss cases pending at SOAH have been remanded to the TDWC since these cases have not been reviewed or decided by the two-prong standard decided by the Third Court of Appeals. The SOAH Administrative Law judges determined that the most appropriate location for these cases is the TDWC, pending a final, non-appealable decision.

A request for rehearing of the Third Court of Appeals decision was denied, but a petition asking the Texas Supreme Court to review the Third Court of Appeals decision is still pending. If the Texas Supreme Court declines a review of or affirms the Third Court of Appeals opinion, final adjudication in these pending stop-loss cases will depend on the uncertain outcome of a very lengthy process. We anticipate further, lengthy litigation at the Travis County District Courts and the Texas Courts of Appeals to establish the legal definition of unusually costly or unusually extensive services. Because of this lengthy process and the uncertainty of recovery in these cases, collection of a material amount of funds in these pending stop-loss cases is not anticipated during the 2010 fiscal year.

Through November 2009, insurance carriers have voluntarily paid the awards in the decisions and orders issued by SOAH, plus interest, in approximately 180 cases, involving approximately $11 million. In most of these cases, the carriers have requested refunds of the payments made in the event that the SOAH decisions and orders are reversed on appeal. We believe the likelihood that the Company will be obligated to refund the payments is remote. Our request that the TDWC Commissioner enforce the awards which have not been voluntarily paid by the carriers has been refused in approximately 130 cases.

Claims regarding payment for hospital outpatient services remain pending at the TDWC. It is expected that these claims will be adjudicated at SOAH and ultimately in the Texas district and appellate courts. The basis for reimbursement for these services made the subject of these pending cases is the determination of fair and reasonable charges. In 2007, we received unfavorable rulings from SOAH in all of our appeals of unfavorable decisions related to services provided in 2001 and 2002. The 179 cases, which have been appealed to the Travis County district courts, challenge the constitutionality of the relevant statutory language. The Company received an unfavorable ruling in its lead case in March 2009, which ruling has been appealed to the Third Court of Appeals. If upheld by the Third Court of Appeals, this ruling will impact cases in which a fee guideline was not applicable, specifically all pending cases involving ambulatory surgical services provided in 2001 and 2002 as well as all pending cases involving hospital outpatient services provided prior to March 1, 2008. Probability of collection in these cases is marginal and depends on the rulings of the Third Court of Appeals.

We are currently pursuing claims against two healthcare agents relating to contracts with certain of our facilities which set out reimbursement guidelines by several workers compensation carriers at a minimum of 70% of the facility s charges. Discovery is continuing on these claims to determine which carriers are involved, the amount of reimbursement due to us, and the data used to determine usual and customary market rates for medical services in specific geographic regions.

Due to the uncertainties regarding the accounts receivable in the MDR process, the 2008 Third Court of Appeals opinion and our legal counsel s advice that settlements with insurance carriers have virtually stopped, the Company had fully reserved all accounts receivable related to the MDR process as of August 31, 2008. Any monies collected for these MDR accounts receivable will be recorded as current period s net patient service revenues.

Table of Contents

Accounts Receivable

Accounts receivable represent net receivables for services provided by the Company. Due to reasons discussed above for writing down all MDR accounts receivable, the Company does not have any long term receivables since August 31, 2008, and expects to collect the net receivables within twelve months from the end of the current period. At each balance sheet date management reviews the accounts receivable for collectibility.

The contractual allowance stated as a percentage of gross receivables at the balance sheet dates is larger than the contractual allowance percentage used to reduce gross billed charges due to the application of partial cash collections to the outstanding gross receivable balances, without any adjustment being made to the contractual allowance. The contractual allowance amounts netted against gross receivables are not adjusted until such time as the final collections on an individual receivable are recognized.

China Division

Revenue Recognition Policy

In China, the local government Department of Health establishes billing rates for a hospital s sale of prescription medication and medical services. A majority of the services provided by Second People s Hospital is to cash pay patients, who pay for the services in advance. For services provided under the local government s social healthcare insurance program, we are generally paid at approximately 95% of billed charges two to three months after the date of service. For the current year, however, receipt of these payments has been delayed due to our acquisition of the management of Second People s Hospital from its prior managers in March 2009. The remaining 5% of billed charges is evaluated by the local government Department of Health on a semi-annual basis and may be paid to the hospital after that evaluation is complete. The Company had bad debt expenses of $1,105 for the quarter ended November 30, 2009 related to denials under the social healthcare insurance program, which is less than 1% of the revenues of the China division for the same period. Since the amount of bad debt expense is minimal, it has been included with other operating expenses in the income statement.

Noncontrolling Interest

The equity of minority investors (minority investors are generally physician groups and other healthcare providers that perform surgeries at the Company s facilities) in certain subsidiaries of the Company is reported on the consolidated balance sheets as noncontrolling interest. Noncontrolling interest reported in the consolidated income statements reflect the respective interests in the income or loss of the limited partnerships or limited liability companies attributable to the minority investors (equity interest ranged from 1.75% to 2.35% at November 30, 2009).

Comprehensive Loss and Accumulated Other Comprehensive Income

Comprehensive loss consists of net loss and other comprehensive income (loss). Other comprehensive income (loss) represents certain components of revenues, expenses, gains and losses that are included in comprehensive loss, but are excluded from net loss. Other comprehensive income (loss) amounts are recorded directly as an adjustment to stockholders equity, net of tax, and for the three months ended November 30, 2009 and 2008 were as follows:

	2009	2008
Net loss	$ (1,332,103)	$ (642,552)
Other comprehensive income (loss), net of taxes:		
Foreign currency translation adjustment, net of taxes of $7,944 and $8,100, respectively	14,753	14,975
Change in valuation of investment available-for-sale, net of taxes of $635,896 and $(97,300), respectively	1,180,950	(180,700)
Total other comprehensive loss, net of taxes	(136,400)	(808,277)
Comprehensive loss attributable to the noncontrolling interest		
Comprehensive loss attributable to Dynacq Healthcare, Inc.	$ (136,400)	$ (808,277)

14

Table of Contents

The components of accumulated other comprehensive income were as follows:

	November 30, 2009	August 31, 2009
Foreign currency translation adjustment, net of taxes of $200,253 and $192,309, respectively	$ 362,279	$ 347,527
Change in valuation of investment available-for-sale, net of taxes of $3,839,947 and $3,204,051, respectively	7,131,331	5,950,381
Total accumulated other comprehensive income, net of taxes of $4,040,200 and $3,396,360, respectively	$ 7,493,610	$ 6,297,908

Contingencies

The Company maintains various insurance policies that cover each of its facilities; including occurrence medical malpractice coverage. In addition, all physicians granted privileges at the Company s facilities are required to maintain medical malpractice insurance coverage. The Company also maintains general liability and property insurance coverage for each facility, including flood coverage. The Company does not currently maintain workers compensation coverage in Texas. In regard to the Employee Health Insurance Plan, the Company is self-insured with specific and aggregate re-insurance with stop-loss levels appropriate for the Company s group size. Coverage is maintained in amounts management deems adequate.

The management agreement for the Second People s Hospital requires that 1% of the drug income, and drug income in excess of 40% of total sales, of the hospital be paid to the government. This requirement was designed to control the cost of drugs by discouraging the sale by the hospital of drugs purchased from other than approved drug vendors. However, the local government has not published a list of approved drug vendors and therefore has not enforced the payment provision since the inception of the original management agreement. The Company has been advised by a local attorney that enforcement of that provision is remote, so it has not accrued the amount that would be payable to the local government if this provision were enforced. If the government were to enforce this provision, Dynacq-Huai Bei could potentially owe approximately $1.2 million to the government for the period of time since inception of the original management contract on the hospital.

The Company is routinely involved in litigation and administrative proceedings that are incidental to its business. Specifically, all judicial review of unsatisfactory determinations of reimbursement amounts due us for our Texas facilities fees must be made in the district courts of Travis County, Texas in what can often be a lengthy procedure. Please refer to Revenue Recognition, as well as Business Government Regulation U.S. Division Texas Workers Compensation Systems in our Form 10-K for the fiscal year ended August 31, 2009, for a detailed description of the MDR process and our accounts receivable. The Company cannot predict whether any litigation or administrative proceeding to which it is currently a party will have a material adverse effect on the Company s results of operations, cash flows or financial condition.

Industry Segments and Geographic Information

We manage our operations through two operating segments, based on our geographic areas: U.S. and China, and have a general corporate division.

U.S. Division

The U.S. Division owns two hospitals, which are the Pasadena facility and the Garland facility. Our U.S. Division develops and operates general acute care hospitals designed to handle specialized surgeries such as bariatric, orthopedic and neuro-spine surgeries. Both of these facilities also provide pain management services, as well as minor emergency treatment services. The Pasadena facility also provides sleep laboratory services.

China Division

Our China Division is set up to provide healthcare management services in China. It includes results of operations for managing Second People s Hospital in Rui An, China, since March 1, 2009.

In 2010 Dynacq-Huai Bei will manage the Third People s Hospital in Rui An upon completion of construction of that hospital.

Table of Contents

The Company has organized Sino Bond Inc. Limited, a Hong Kong corporation (Sino Bond), to hold and manage investments in Hong Kong. Sino Bond has entered into a three-year marketing contract effective October 1, 2008 for marketing of healthcare services to be provided by Dynacq subsidiaries in China and Southeast Asia.

In August 2009 the Company organized Hu GangJing (Hang Zhou) Technology Co. Ltd. (Hang Zhou Tech) under the laws of the People s Republic of China for the purpose of forming joint ventures to invest in companies in China engaged in businesses such as energy production, life sciences and pharmaceuticals.

Corporate Division

The Company has invested in available-for-sale securities which will be held until the Company is able to identify and fund attractive opportunities to acquire or manage operating companies in China and Southeast Asia. Corporate division includes interest and other income related to these investments in available-for-sale securities, corporate personnel compensation expenses, and general and administrative expenses. Such expenses and income are not allocated to our operating divisions, as they relate to our general corporate activities.

We generally evaluate performance based on profit or loss from operations before income taxes and non-recurring charges and other criteria. The accounting policies of the reportable segments are the same as those described in the summary of significant accounting policies. There are no transfers between segments.

Summarized financial information concerning the business segments from continuing operations is as follows:

	Three Months Ended November 30,	
	2009	**2008**
Revenues from external customers		
Net patient service revenues		
U.S. Division	$ 8,385,229	$ 10,879,238
China Division	599,382	
Consolidated	$ 8,984,611	$ 10,879,238
Income (loss) before taxes		
U.S. Division	$ (659,662)	$ 464,009
China Division	(425,073)	(465,148)
Corporate	(888,733)	(904,231)
Consolidated	$ (1,973,468)	$ (905,370)

	November 30,	
	2009	**2008**
Total Assets		
U.S. Division	$ 37,722,049	$ 42,800,667
China Division	25,744,312	28,913,405
Corporate	20,870,851	3,628,000
Consolidated	$ 84,337,212	$ 75,342,072

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

This quarterly report on Form 10-Q contains forward-looking statements. In some cases, you can identify forward-looking statements by terminology such as may, will, should, expects, intends, plans, anticipates, believes, estimates, predicts, potential, or the ne or other comparable terminology. These statements are only predictions. Actual events or results may differ materially. Such forward-looking statements relate to future events or future financial performance and involve known and unknown risks, uncertainties and other factors that may cause our Company s actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by the forward-looking statements, including the risks and uncertainties described in Risk Factors in our annual report on Form 10-K for the fiscal year ended August 31, 2009. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of

16

activity, performance, or achievements. You must read the following discussion of the results of our business and our operations and financial condition in conjunction with our reviewed consolidated financial statements, including the notes, included in this quarterly report on Form 10-Q and our audited consolidated financial statements, including the notes, included in our Annual Report on Form 10-K for the fiscal year ended August 31, 2009.

Update on Critical Accounting Policies and Estimates

There have been no changes to the critical accounting policies used in our reporting of results of operations and financial position for the quarter ended November 30, 2009. For a discussion of our critical accounting policies see Management s Discussion and Analysis of Financial Condition and Results of Operations in our Form 10-K for the fiscal year ended August 31, 2009.

Table of Contents

Results of Operations

	Three Months Ended November 30, 2009							Three Months Ended November 30, 2008					
	U.S. Division		**China Division**		**Corporate**	**Total**		**U.S. Division**		**China Division**	**Corporate**	**Total**	
Net patient service revenue	$ 8,385,229	100%	$ 599,382	100%	$	$ 8,984,611	100%	$ 10,879,238	100%	$	$	$ 10,879,238	100%
Costs and expenses:													
Compensation and benefits	3,198,213	38	298,821	50	584,873	4,081,907	45	3,260,112	30	37,500	383,928	3,681,540	34
Medical services and supplies	2,414,634	29	304,869	51		2,719,503	30	3,289,820	30			3,289,820	30
Other operating expenses	3,292,396	39	687,510	115	703,904	4,683,810	52	3,623,466	33	491,777	520,303	4,635,546	43
Depreciation and amortization	235,585	3	30,394	5		265,979	3	376,655	3	17,569		394,224	4
Total costs and expenses	9,140,828	109	1,321,594	220	1,288,777	11,751,199	131	10,550,053	97	546,846	904,231	12,001,130	110
Operating income (loss)	(755,599)	(9)	(722,212)	(120)	(1,288,777)	(2,766,588)	(31)	329,185	3	(546,846)	(904,231)	(1,121,892)	(10)
Other income (expense):													
Rent and other income	90,633	1	258,985	43		349,618	4	71,678	1			71,678	1
Interest income	16,697		38,154	6	400,044	454,895	5	74,143	1	81,698		155,841	1
Interest expense	(11,393)					(11,393)		(10,997)				(10,997)	
Total other income, net	95,937	1	297,139	50	400,044	793,120	9	134,824	1	81,698		216,522	2
Income (loss) before income taxes	(659,662)	(8)%	(425,073)	(71)%	(888,733)	(1,973,468)	(22)	464,009	4%	(465,148)	(904,231)	(905,370)	(8)
Benefit for income taxes						621,896	7					261,464	2
Net loss						(1,351,572)	(15)					(643,906)	(6)
Less: Net loss attributable to the noncontrolling interest						19,469						1,354	
Net loss attributable to Dynacq Healthcare, Inc.						$ (1,332,103)	(15)%					$ (642,552)	(6)%

Operational statistics (Number of medical procedures) for U.S. Division:		
Inpatient:		
Bariatrics	39	157
Orthopedics	89	61
Other	37	44
Total inpatient procedures	165	262
Outpatient:		
Orthopedics	152	175
Other	323	371
Total outpatient procedures	475	546
Total procedures	640	808

Table of Contents

Three Months Ended November 30, 2009 Compared to the Three Months Ended November 30, 2008

U.S. Division

Net patient service revenue decreased by $2,494,009, or 23%, from $10,879,238 to $8,385,229, and total surgical cases decreased by 21% from 808 cases in 2008 to 640 cases in 2009. Following are the percentage changes in net patient service revenues and number of cases at the hospital facilities:

	Percentage increase (decrease) from 2008 to 2009	
Facility	**Net patient revenue**	**Cases**
Pasadena	56%	23%
Garland	(56)	(50)
Overall	(23)	(21)

The decrease in net patient service revenue was due to an overall decrease in number of cases by 21% in 2009 compared to 2008. There was a significant decrease of 37% in inpatient cases, which typically have higher average reimbursement per case compared to outpatient cases. Gross billed charges and net patient service revenues were negatively impacted by Hurricane Ike in the month of September 2008 for our Pasadena facility, which was not in full operation for about three weeks.

Total costs and expenses decreased by $1,409,225 or 13%, from $10,550,053 in 2008 to $9,140,828 in 2009. The following discusses the various changes in costs and expenses:

Compensation and benefits decreased marginally by $61,899, or 2%, primarily due to lower net patient service revenues.

Medical services and supplies expenses decreased by $875,186, or 27%, while the number of surgery cases decreased 21%. The percentage decrease in medical services and supplies was higher than the percentage decrease in the number of surgery cases due to a 37% decrease in inpatient cases, which typically require more medical services and supplies.

Other operating expenses decreased by $331,070, or 9%. Marketing expenses, included in other operating expenses, decreased marginally by $31,000 from $1,531,000 in 2008 to $1,500,000 in 2009. Other operating expenses, excluding marketing expenses, as a percentage of gross billed charges were constant at 6.4% and 5.4% for 2009 and 2008, respectively.

China Division

For the quarter ended November 30, 2009, Second People s Hospital had net patient service revenues of $599,382, with no such corresponding revenues in the prior period. The contract to manage the Second People s Hospital in Rui An, China was executed in March 2009.

Total costs and expenses for the China Division increased by $774,748, from $546,846 in 2008 to $1,321,594 in 2009. In 2009, total costs and expenses includes the operations associated with Second People s Hospital in Rui An, China.

Corporate Division

The Corporate division includes interest and other income related to the investments in available-for-sale securities, corporate personnel compensation expenses and general and administrative expenses. Such expenses and income are not allocated to our operating divisions, as they relate to our general corporate activities. Corporate costs

Table of Contents

and expenses increased by $384,546 from $904,231 in 2008 to $1,288,777 in 2009, due to increases in personnel costs and other operating expenses. Interest income of $400,044 in 2009 relates to the investments in available-for-sale securities, which were purchased at a cost of $9,135,146 and have appreciated in fair value by an additional $11,253,870. Of that amount, $282,608 in foreign exchange gains was included in rent and other income in the Consolidated Statement of Operations for the fiscal year ended August 31, 2009. Unrealized gains in these investments of $10,971,278 are included in accumulated other comprehensive income in the Consolidated Balance Sheet, net of taxes of $3,839,947.

Liquidity and Capital Resources

Our 2009 Annual Report on Form 10-K includes a detailed discussion of our liquidity, contractual obligations and commitments. The information presented below updates and should be read in conjunction with the information disclosed in that Form 10-K.

Cash flow from operating activities

Total cash flow used in operating activities was $2,754,973 during the period ended November 30, 2009, primarily due to a net loss of $1,332,103, decreases in accounts payable and accrued liabilities of $960,351, changes in income tax related accounts of $949,301, partially offset by decreases in accounts receivable of $632,204 and depreciation and amortization of $265,979.

Cash flow from investing activities

Total cash flow used in investing activities was $309,230 for purchase of equipment.

Cash flow from financing activities

Total cash flow used in financing activities was $474,895 primarily related to treasury stock purchases of $373,327 and $124,626 payments on the note payable for class action lawsuit settlement.

The Company had working capital of $38,956,574 as of November 30, 2009, and maintained a liquid position by a current ratio of approximately 5.3 to 1.

We believe we will be able to meet our ongoing liquidity and cash needs for fiscal year 2010 through the combination of available cash and cash flow from operations.

Recent Accounting Pronouncements

In December 2007, the Financial Accounting Standards Board issued Accounting Standards Codification (ASC) Topic 805-10, Business Combinations (formerly referred to as SFAS No. 141 (revised 2007)) and ASC Topic 810-10, Consolidation (formerly referred to as SFAS No. 160, Noncontrolling Interest in Consolidated Financial Statements). These new standards represent the outcome of the FASB s joint project with the International Accounting Standards Board and are intended to improve, simplify and converge internationally the accounting for business combinations and the reporting of noncontrolling interests in consolidated financial statements.

ASC Topic 805-10 replaces SFAS No. 141, Business Combinations, however, it retains the fundamental requirements of the former Statement that the acquisition method of accounting (previously referred to as the purchase method) be used for all business combinations and for an acquirer to be identified for each business. This Statement defines the acquirer as the entity that obtains control of one or more businesses in the business combination and establishes the acquisition date as the date that the acquirer achieves control. The new standard requires the acquiring entity in a business combination to recognize all (and only) the assets acquired and liabilities assumed in the transaction; establishes the acquisition-date fair value as the measurement objective for all assets acquired and liabilities assumed; and requires the acquirer to disclose to investors and other users all of the information they need to evaluate and understand the nature and financial effect of the business combination.

Table of Contents

ASC Topic 810-10 amends Accounting Research Bulletin No. 51, Consolidated Financial Statements, to establish accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. This Statement clarifies that a noncontrolling interest in a subsidiary is an ownership interest in the consolidated entity that should be reported as equity in the consolidated financial statements. This Statement changes the way the consolidated income statement is presented by requiring net income to be reported at amounts that include the amounts attributable to both the parent and the noncontrolling interest and to disclose those amounts on the face of the income statement. It also aligns the reporting of noncontrolling interest in subsidiaries with the requirements in International Accounting Standard 27.

The Company adopted the provisions of both ASC Topic 805-10 and ASC Topic 810-10 effective September 1, 2009, and its adoption did not have a material impact on our consolidated financial statements.

In April 2009, the FASB issued ASC Topic 820-10, Fair Value Measurements & Disclosures (formerly referred to as FASB Staff Position No. 157-4, Determining Fair Value When the Volume and Level of Activity for the Asset or Liability has Significantly Decreased and Identifying Transactions That Are Not Orderly) and ASC Topic 320-10, Investments Debt and Equity Securities (formerly referred to as FASB Staff Position No. 115-2 and 124-2, Recognition and Presentation of Other-Than-Temporary Impairments). These two ASC Topics were issued to provide additional guidance about (1) measuring the fair value of financial instruments when the markets become inactive and quoted prices may reflect distressed transactions, and (2) recording impairment charges on investments in debt instruments. Additionally, the FASB issued ASC Topic 825-10-65, Financial Instruments (formerly referred to as FASB Staff Position No. 107-1 and APB 28-1, Interim Disclosures about Fair Value of Financial Instruments) to require disclosures of fair value of certain financial instruments in interim financial statements. All of these ASC Topics were adopted in the fourth quarter of fiscal year ended August 31, 2009.

In May 2009, the FASB issued ASC Topic 855-10, Subsequent Events (formerly referred to as SFAS 165), which establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. The adoption in the fourth quarter of fiscal year 2009 did not have any material impact on the Company s consolidated financial statements. For the quarter ended November 30, 2009, the Company evaluated subsequent events through January 12, 2010, the date the consolidated financial statements were issued.

In June 2009, the FASB issued ASC Topic 105-10, Generally Accepted Accounting Principles , (formerly referred to as SFAS No. 168, The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles). ASC Topic 105-10 establishes the ASC as the source of authoritative non-governmental generally accepted accounting principles (GAAP). The Company adopted the provisions of this statement effective September 1, 2009, and its adoption did not have a material impact on the Company s consolidated financial statements, though it changed references of accounting literature disclosed in the notes to the consolidated financial statements.

In September 2009, the FASB issued Accounting Standards Update (ASU) 2009-06, Implementation Guidance on Accounting for Uncertainty in Income Taxes and Disclosure Amendments for Nonpublic Entities . ASU 2009-06 provides additional implementation guidance on accounting for uncertainty in income taxes and eliminates the disclosures required by paragraph ASC Topic 740-10-50-15(a) through (b) for nonpublic entities. The Company adopted the provisions of ASU 2009-09, and its adoption did not have a material impact on its consolidated financial statements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Not required.

Item 4T. Controls and Procedures.

Under the supervision and with the participation of our management, including our chief executive officer and chief financial officer, we conducted an evaluation to assess the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report, pursuant to Exchange Act Rule 13a-15(e). Based on that evaluation, our chief executive officer and chief financial officer concluded that, as of November 30, 2009, our internal disclosure controls and procedures were effective.

Table of Contents

There have been no significant changes in our internal control over financial reporting during the most recently completed fiscal quarter or in other factors that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings.

The Company is routinely involved in litigation and administrative proceedings that are incidental to its business. Specifically, all judicial review of unsatisfactory determinations of reimbursement amounts due us for our Texas facilities fees must be made in the district courts of Travis County, Texas in what can often be a lengthy procedure. Please refer to Revenue Recognition, as well as Business Government Regulation U.S. Division Texas Workers Compensation Systems in our Form 10-K for the fiscal year ended August 31, 2009, for a detailed description of the MDR process and our accounts receivable. The Company cannot predict whether any litigation or administrative proceeding to which it is currently a party will have a material adverse effect on the Company s results of operations, cash flows or financial condition.

Item 1A. Risk Factors.

The Company s Risk Factors as disclosed in its Form 10-K for the year ended August 31, 2009 have not changed.

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

Purchases of Equity Securities by the Company

On February 29, 2008 the Company s Board of Directors authorized a program of repurchasing up to 2 million of its outstanding securities from time to time in open market transactions at prevailing prices on NASDAQ. Shares repurchased during the quarter ended November 30, 2009 pursuant to our repurchase program are as follows:

Period	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Average Price per Share	Maximum Number of Shares that May Yet be Purchased Under the Publicly Announced Plans or Programs
September 1 30, 2009	51,110	$ 3.46	1,385,339
October 1 31, 2009	31,610	3.49	1,353,729
November 1 30, 2009	24,960	3.46	1,328,769
Total	107,680	$ 3.47	1,328,769

Item 3. Defaults Upon Senior Securities.

None.

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

None.

Item 5. Other Information.

None.

Item 6. Exhibits.

EXHIBIT NO.	**IDENTIFICATION OF EXHIBIT**
Exhibit 15.1	Awareness Letter of Killman, Murrell & Company, P.C.
Exhibit 23.1	Consent of Killman, Murrell and Company, P.C.
Exhibit 31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
Exhibit 31.2	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
Exhibit 32.1	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
Exhibit 32.2	Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

Table of Contents

SIGNATURES

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

DYNACQ HEALTHCARE, INC.

Date: January 12, 2010	By: /s/ Chiu M. Chan Chiu M. Chan Chief Executive Officer (duly authorized officer)
Date: January 12, 2010	By: /s/ Philip S. Chan Philip S. Chan Chief Financial Officer (principal financial and accounting officer)

Table of Contents

INDEX OF EXHIBITS

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