

Testimony of
Kelvyn Cullimore Jr., President and CEO of Dynatronics
U.S. House of Representatives
Committee on Oversight and Government Reform's
Subcommittee on Health Care and D.C.

Thank you Chairman Gowdy and Ranking Member Davis for the opportunity to testify here today. My name is Kelvyn Cullimore. I am the President and CEO of Dynatronics Corporation. I also serve on the board of the Medical Device Manufacturers Association and am a Trustee of the Utah Technology Council. Dynatronics is a NASDAQ listed company engaged in the manufacture and distribution of medical devices and products primarily for physical therapy and sports medicine applications. We have a manufacturing facility and corporate headquarters in Cottonwood Heights, Utah a suburb of Salt Lake City, where we manufacture high tech electronic devices and employ about 70 people. We also have a facility in Chattanooga, TN where we employ 46 people in manufacturing hot packs, cold packs, treatment tables and other similar products that we both manufacture and import. We have 14 employees at satellite sales and staging offices in Detroit, MI, Pleasanton, CA, Youngstown, OH, Minneapolis, MN, and Houston, TX. We are one of two companies left in our market niche that has a direct sales force with 50 direct sales representatives scattered around the country. Including all direct sales reps, we provide employment for over 180 people.

Dynatronics is a relatively small company with sales of about \$32M. But that is common in this industry. A majority of medical device companies are small companies. Many are in the early stages of product development with sales, but no profits. My father and I started Dynatronics over 30 years ago. We have had good years, but the last few years have been a struggle. Like many companies facing difficult economic conditions, we have been required to implement several rounds of layoffs to reduce expenses. In such a difficult economic environment it is doubly hard to accept the imposition of a new tax that will further hamper our ability to innovate and provide jobs for the number of people we have traditionally employed.

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Despite widespread economic challenges, I consider myself extremely fortunate to be a part of a generally vibrant industry that plays a critical role in improving healthcare in this country. The medical device industry is comprised of over 400,000 highly skilled and science-driven professionals, with well over 1 million jobs that are part of our industry supply chain. Including other support and related business, there are over 2 million hard working Americans who drive this proud success story, and one where the United States is the global leader (2010, State of the Industry, The Lewin Group). The most recent data from the Department of Commerce shows that the medical device industry exported \$36 billion of products in 2010 and had a trade surplus of approximately \$3.2 billion. Few segments of the United States economy can lay claim to a trade surplus.

Since I first joined the medical device industry over 30 years ago, that is a statistic that has been widely touted; that we are the global leader in medical technology innovation. This is probably not the first time you have heard this, but I want to be very clear that the United States is in very real danger of losing our leadership position, and if this happens, it will be virtually impossible to get this position back as capital and human resources flow to new centers of innovation out of our country. The challenges of an uncertain regulatory environment, reimbursement pressures, and of course the medical device tax, among others, have created what many who have testified in Congress before describe as a “perfect storm.” I am here today to share the sobering news that this “perfect storm” could lead to a Class 5 hurricane for patients, providers and industry.

The Dynatronic’s story in this current environment is not really unique, but it is illustrative of how harmful policies such as the 2.3% medical device tax in the Affordable Care Act are to our ability to improve patient care and drive job creation.

Our fiscal year just ended on June 30th. We will report sales in excess of \$32,000,000 but for only the fourth time in 25 years will not be profitable. After reporting a pre-tax profit of just over \$400,000 last year, we will report a pre-tax

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loss of just under \$300,000 for this fiscal year. The reduction in profitability is due to slightly lower sales and increased R&D expenses. The profit last year represented 1.2% of sales. If the 2.3% medical device EXCISE tax was in place last year – which as you know is a tax on revenue, regardless of profitability – we would have owed the IRS hundreds of thousands of dollars in excise taxes significantly reducing or even eliminating our profits. Worse than this would be the scenario for the most recent fiscal year wherein we expect to show a loss of just under \$300,000. For our effort, we would still be obligated to pay the IRS approximately the same hundreds of thousands of dollars in excise taxes despite not being profitable.

Quite simply, a company such as ours and thousands of others that are similarly struggling, or have not yet crested the hill of profitability as a start-up company, will have a VERY difficult decision to make in addressing this added tax. Where do I get the money to pay the tax? How do I return to past levels of profitability? How do I keep my company viable? Research and development are the easiest short term cuts but they lead to less innovation and growth. Do I reduce employee benefits? Do I drop product lines that are marginally profitable that now are no longer profitable due to the tax? This would reduce employment but possibly save expenses.

Some would say that we offset the tax by raising our prices. Pass it along to the end user. Anyone operating in the current environment knows that there is no appetite on the part of hospitals and practitioners to accept price increases of any kind. To the contrary, we are under tremendous pressure to lower prices. Much of what we manufacture is capital equipment. Capital equipment is only replaced if there is something significantly more innovative or if the products are wearing out. In this environment, practitioners and facilities are extending the useful life of their devices and equipment and if R&D is cut, innovation will suffer. Increasing prices to cover the medical device tax will not encourage practitioners to open their wallets to purchase new devices – not to mention that larger, more financially

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strong competitors can absorb the tax better than the small companies like Dynatronics.

There is also talk that adding millions to the rolls of the insured will bring more patients needing care, thus more business for those paying the tax. That may be comfortable rhetoric for justifying the imposition of the tax, but at least in our case, and in the case of many like us, we do not expect the additional coverage to increase sales of our products. Existing capital equipment may get used more, but it will not necessitate the purchase of additional capital equipment. It may help with those who sell consumable products, but not capital products. Besides, many of those newly insured being added were already accessing necessary care through existing charitable and emergency room channels. The real increase in demand for medical products is expected to be modest at best and mostly affecting consumable type products. This dynamic is currently being validated in the state of Massachusetts where near universal health insurance exists and yet manufacturers have not experienced a significant increase utilization of their products and services.

In our particular case, there is also the current effort by Congress to put caps on reimbursement for physical therapy services. If the caps are imposed, revenue for physical therapists will diminish leaving even fewer resources for the purchase of new or additional capital equipment and supplies. As a company we are being squeezed in a legislative vice between capped reimbursements for physical therapy services and being assessed the medical device excise tax on sales of manufactured products. It will eventually crush us.

Regardless of a company's size, success or stage of development for medical technologies, a 2.3% excise tax will have a significant impact, and hurt patients and providers at the end of the day. What is unique about our innovative industry as a whole is that it is comprised overwhelmingly of small companies. It is estimated that 80 percent have less than 50 employees. While Dynatronics is fortunate to have existing devices and products on the market to generate revenue

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and hopefully a return to profitability, the majority of device companies are pre-profit and struggling to get to the point where they can begin to recover the millions of dollars spent on research, clinical trials and other development costs.

Most importantly, what does this mean to patients and providers? Sadly, policies such as the medical device tax are placing huge hurdles to delivering on the promises of improved patient care and a better quality of life.

For example, my company has devices and technologies in hospitals, therapy centers and facilities throughout the United States, being used on average by tens of thousands of patients every day. If a company such as Dynatronics decides to address the device tax by making severe cuts to R&D, what I have essentially done is limited the potential for my company to have new technologies and devices in place 3-5 years down the road. I cannot emphasize enough just how delicate the innovation ecosystem is for medical device makers. Any cuts to R&D today will manifest themselves down the road in ways that hurt patients and providers the most.

Think of all the amazing technologies and procedures we read about today: Aortic stents, dialysis machines, surgical robotics and so many more.

Despite the unbelievable amount of innovation and ingenuity it took to deliver these life-changing technologies, many of us take it for granted that these amazing tools are available for providers to help patients.

But imagine if the medical device tax was implemented in 2003 instead of 2013. How many small and innovative companies would simply have folded due to an inability to generate profit in a reasonable time? How many jobs would have been lost, adding to the roles of the unemployed and uninsured? How many cuts to R&D would have been made leading to unknown losses in innovation and patient care? Would all the cutting edge devices and technologies developed over the past decade really be available today?

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Some have tried to minimize the impact of the device tax saying it is only 2.3% of sales as though that number is insignificant. It is not. Most medical device companies will operate on profit margins averaging 5-7% of sales. As a percentage, 2.3% is the equivalent of 33-45% tax. Imagine further trying to attract needed capital from investors and explaining that the first 2.3 dollars of every hundred in sales is paid to the government before the investors receive anything. Not only does this chill investment in medical device technology as investment dollars seek other venues not so burdened, but it makes the hill to profitability for innovative start-up companies that much harder to climb. And for those already established, it will reduce the return to investors and the price-earnings ratio for those who have the misfortune of being a public company. This tax will reduce their market cap, discourage investors and affect millions of shareholders who will lose value in their stock as profits potentially decline and the market absorbs the impact of this tax. The consequences of taxing medical device companies to support broader public policy relative to more universal health care reform are not insignificant and will be far reaching relative to future innovation and expansion of this industry.

It is often said that while we fear the known obstacles in our lives, it is the unknown ones that can present the greatest challenges. The impact of the medical device tax and various other unreasonable policies in the Affordable Care Act will clearly have a negative impact on innovation and patient care, but to what degree is unknown. We DO know that it has already led to job losses; we DO know that companies have already stated they are cutting back on R&D; and we DO know that it has been identified as a major factor in the steady decline in investments and venture capital to young start-ups in this crucial field of innovation.

The United States simply cannot lose our leadership position in something as important as patient care. The jobs the medical device innovators create are great, the technologies and devices being developed literally are changing lives each and every day, and we all recognize that we need to improve outcomes and drive down

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the costs of care. Medical device innovation plays a central role in patient care, but we face many headwinds and need your help to temper the headwinds and avoid the creation of that Category 5 hurricane.

Dynatronics is but one example of a Company that faces an extreme challenge in coping with the burden of this tax combined with the other economic factors we are confronting including reduced reimbursements. The perfect storm is becoming a Class 5 hurricane for us. We will fight to preserve what we have built over the past 30 years. We will fight to save as many jobs as we can. We will not willingly be sacrificed at the altar of universal health care as an unfortunate casualty for the greater good. But it will require significant restructuring that will inevitably include loss of jobs and reduction in research and development. Industry-wide, this will ultimately and unfortunately have a dire impact on patient care and the tools providers have at their disposal.

I respectfully urge our national leaders to work together to provide an environment where tomorrow's technologies and devices will not be sacrificed for misguided policies today. America's patients, providers and workers are counting on it.
Thank you.

BIOGRAPHICAL INFORMATION ON KELVYN H. CULLIMORE JR.

Kelvyn H. Cullimore Jr. presently serves as Chairman, President & CEO of Dynatronics Corporation, a publicly traded medical device manufacturer with headquarters in Cottonwood Heights, Utah. He has served as a Director and Officer of Dynatronics since it was founded by him and his father in 1979. Prominent in the physical therapy market, Dynatronics is known for its advanced technology electrotherapy and ultrasound devices, pain management systems and aesthetic products. Dynatronics equipment is used by top therapists and trainers with a majority of professional sports franchises and college teams owning Dynatronics products.

In 2003, Mr. Cullimore joined the board of directors of the Medical Device Manufacturers Association headquartered in Washington, D.C. and currently serves on its executive committee. He is a Trustee of the Utah Technology Council which is an industry association for life science and high tech companies.

In addition to his professional career, Mr. Cullimore also serves as the Mayor of Cottonwood Heights, UT. Mayor Cullimore was elected the first Mayor of Cottonwood Heights in November, 2004. From 2002-2004, Mayor Cullimore worked as a member of the committee to incorporate Cottonwood Heights as the 16th city in Salt Lake County.

In addition to his mayoral duties starting up a new city of approximately 36,000 residents, Mayor Cullimore is a member of the board of the largest fire agency in Utah, the Unified Fire Authority, serving as the chairman of its finance committee. He has served as President of the Salt Lake County Council of Governments the Salt Lake County Conference of Mayors, He also serves on numerous other County-wide committees including chair of the County Advisory Board on Tourism, Recreation, Convention, and Cultural activities. Mayor Cullimore was a recipient of the Best of State Award in 2008 as the Best Elected Official.

Mr. Cullimore has served in many positions for the Boy Scouts of America, including Scoutmaster, and in 2002 received the District Award of Merit for his service.

He graduated cum laude from Brigham Young University in 1980 with a degree in Financial and Estate Planning. Kelvyn and his wife, Laurie Lyn Cullimore, are the parents of five children, five grandchildren and have lived in Cottonwood Heights since 1980.

Committee on Oversight and Government Reform
Witness Disclosure Requirement - "Truth in Testimony"
Required by House Rule XI, Clause 2(g)(5)

Name: Kelvyn H. Willimore Jr

1. Please list any federal grants or contracts (including subgrants or subcontracts) you have received since October 1, 2009. Include the source and amount of each grant or contract.

I have not received any grants or contracts since October 1, 2009.

In addition to my position as President & CEO of Dynatronics Corp who I will be representing in connection with my testimony, I also serve as the Mayor of Cottonwood Heights, UT. The city has received law enforcement and transportation grants. A list of such grants can be provided upon request.

2. Please list any entity you are testifying on behalf of and briefly describe your relationship with these entities.

I am testifying as the president & CEO of Dynatronics Corporation, a Utah based manufacturer of medical devices for Physical Therapy

3. Please list any federal grants or contracts (including subgrants or subcontracts) received since October 1, 2009, by the entity(ies) you listed above. Include the source and amount of each grant or contract.

No grants have been received by Dynatronics since Oct 1, 2009.

I certify that the above information is true and correct.

Signature: Kelley

Date: 7/6/2012