

NATUS MEDICAL INC  
Form 10-K/A  
May 22, 2008  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**

**FORM 10-K/A**  
**(Amendment No. 1)**

(Mark One)

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the Fiscal Year Ended December 31, 2007

OR

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

Commission File Number: 000-33001

**Natus Medical Incorporated**

(Exact name of registrant as specified in its charter)

**Delaware**  
(State or Other Jurisdiction of Incorporation or Organization)

**77-0154833**  
(I.R.S. Employer Identification No.)

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1501 Industrial Road, San Carlos, California 94070

(Address of principal executive offices, including zip code)

(650) 802 0400

(Registrant's Telephone Number, including area code)

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act: Common Stock, \$0.001 par value

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K/A or any amendment to this Form 10-K/A.

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 definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer

Accelerated Filer

Non-Accelerated Filer  (Do not check if a smaller reporting company)

Smaller reporting company

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

As of June 30, 2007, the last business day of the registrant's most recently completed second fiscal quarter, there were 21,636,590 shares of Registrant's common stock outstanding, and the aggregate market value of such shares held by non-affiliates of Registrant (based upon the closing sale price of such shares on the Nasdaq Global Market on July 2, 2007) was \$240,110,035. Shares of Registrant's common stock held by each executive officer and director and by each entity that owns 5% or more of Registrant's outstanding common stock have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

On March 7, 2008, the Registrant had 21,768,855 shares of its common stock outstanding.

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**Explanatory Note**

This Amendment No. 1 on Form 10-K/A (this Amendment) amends our Annual Report on Form 10-K for the year ended December 31, 2007, originally filed with the Securities and Exchange Commission on March 14, 2008 (the Original Filing). This Amendment is being filed to revise information in Items 1, 7, 11 and 12, which are amended and restated in their entirety as contained in this Amendment. Item 1 is being revised to replace the Natus Medical Product Families chart with a corrected version. Item 11 is being revised to correct disclosure of (1) the values of stock and option awards we granted to our named executive officers, as set forth in the summary compensation table and grants of plan based awards table, (2) salary information for one of our executive officers, as set forth in the summary compensation table, and (3) the number of shares subject to outstanding options held by one of our directors, the amount paid prior to October 2007 as an annual retainer to the Chairman of the Company's Compensation Committee and to correct the grant date fair value of the options granted to our non-employee directors in 2007, as set forth in the director compensation table. Item 12 is being revised to add footnote disclosure that one of our executive officers and one of our directors have pledged their shares.

This Amendment continues to speak as of the date of the Original Filing, as we have not updated the disclosures contained in the Original Filing to reflect any events that occurred at a later date, other than the updating of the exhibits to include updated Certifications of our Chief Executive Officer and Chief Financial Officer.

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### **ITEM 1. Business.**

*This Annual Report on Form 10-K/A contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 about Natus Medical Incorporated ( Natus, we, us, or our Company ). These statements include, among other things, statements concerning our expectations, beliefs, plans, intentions, future operations, financial condition and prospects, and business strategies. The words may, will, continue, estimate, project, intend, believe, expect, anticipate, and other similar expressions generally identify forward-looking statements. Forward-looking statements in this Item 1 include, but are not limited to, statements regarding the effectiveness and advantages of our products, factors relating to demand for and economic advantages of our products, our plan to develop and acquire additional technologies, products or businesses, and our marketing, technology enhancement, and product development strategies.*

*Forward-looking statements are not guarantees of future performance and are subject to substantial risks and uncertainties that could cause the actual results to differ materially from those that we predicted in the forward-looking statements. Investors should carefully review the information contained under the caption Risk Factors contained in Item 1A for a description of risks and uncertainties that could cause actual results to differ from those that we predicted. All forward-looking statements are based on information available to us on the date hereof, and we assume no obligation to update forward-looking statements.*

*Natus®, AABR®, ABAer®, ALGO®, AuDX®, Biliband®, Bio-logic®, Ceegraph®, CHAMP®, Cool-Cap®, Ear Couplers®, Flexicoupler®, MASTER®, Navigator®, neoBLUE®, Oxydome®, Sleepscan®, Smart Scale®, Traveler®, Warmette® and VAC-PAC® are registered trademarks of Natus Medical Incorporated. Accuscreen®, Bili-Lite Pad®, Bili-Lite®, Billi-Bassinet®, Bili-Mask®, Bili-Meter®, Circumstraint®, EchoLink®, MiniMuffs®, Neometrics®, Papoose Board®, Smartpack® and Warm-Lamp® are non-registered trademarks of Natus. Solutions for Newborn Care® is a non-registered service mark of Natus. Deltamed® and Coherence® are registered trademarks of Deltamed SA. Fischer-Zoth®, AOAE®, Cochlea-Scan® and Echo-Screen® are registered trademarks of Fischer-Zoth GmbH. Sleeprite® is a registered trademark of Excel Tech Ltd. Neuromax® and Xltek® are non-registered trademarks of Excel Tech Ltd.*

### **Overview**

Natus is a provider of healthcare products used for the screening, detection, treatment, monitoring and tracking of common medical ailments such as hearing impairment, neurological dysfunction, epilepsy, sleep disorders, and certain newborn conditions. We develop, manufacture, and market advanced neurodiagnostic and newborn care products to healthcare professionals in over 80 countries. Our product offerings include computerized neurodiagnostic systems for audiology, neurology, polysomnography, and neonatology, as well as newborn care products such as hearing screening systems, phototherapy devices for the treatment of newborn jaundice, head-cooling products for the treatment of brain injury in newborns, and software systems for managing and tracking disorders and diseases for public health laboratories.

We have completed a number of acquisitions since 2003, consisting of either the purchase of a company, substantially all of the assets of the company, or individual products or product lines. The businesses we have acquired include Neometrics in 2003, Fischer-Zoth in 2004, and Bio-logic, Deltamed, and Olympic in 2006. On November 29, 2007 we acquired Excel-Tech Ltd. ( Xltek ), based in Oakville, Ontario, Canada. Xltek develops and markets computer-based electrodiagnostic systems and disposable supplies used by medical practitioners to aid in the detection, diagnosis, and monitoring of neurologic and sleep disorders.

### **Product Families**

We categorize our products into the following product families:

**Hearing** Includes product lines for Newborn Hearing Screening and Diagnostic Hearing Assessment.

**Monitoring Systems for Neurology** Includes product lines for Diagnostic Neurologic Analysis (EEG), Diagnostic Sleep Analysis (PSG), Electromyography (EMG), Intra-operative Monitoring (IOM); and Newborn Brain Monitoring (CFM).

**Newborn Care** Includes products for the treatment of Brain Injury and Jaundice in newborns.



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Our principal product offerings within these product families are presented in the table below:

### **Our Product Offerings**

#### **Hearing**

##### *Newborn Hearing Screening*

###### *Overview*

Hearing impairment is the most common treatable chronic disorder in newborns, affecting as many as five babies out of every 1,000 newborns. It is estimated that 20,000 hearing-impaired babies are born in the United States ( U.S. ) every year, and as many as 60,000 more in the rest of the developed world. Until the introduction of universal newborn hearing screening programs, screening was generally performed only on those newborns who had identifiable risk factors for hearing impairment. However, screening only those newborns with risk factors for hearing impairment overlooks approximately half of newborns with some level of hearing impairment.

Early identification of hearing impairment and early intervention has been shown to improve language development significantly. Undetected hearing impairment often results in the failure to learn, process spoken language, and speak. If hearing impairment is not detected prior to discharge from the hospital it is often not detected until the child is 18 months of age or older. A 1997 study conducted at the University of Colorado, Boulder evaluated the impact of hearing impairment on language and speech. All of the children evaluated in the study were born with a hearing impairment but differed by the age at which the hearing impairment was detected. The study concluded that those children whose hearing loss was detected early and who received appropriate treatment had significantly better language skills and vocabularies than those children whose hearing loss was detected later.

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### *Newborn Hearing Screening in the United States*

We estimate that today approximately 95% of the children born in the U.S. are being screened for hearing impairment prior to discharge from the hospital. In 1994, the American Academy of Pediatrics Task Force on Newborn and Infant Hearing first published specific guidelines for universal newborn hearing screening programs. In 2000 and 2007, the Joint Committee on Infant Hearing ( JCIH ) Position Statements outlined principles, guidelines, and benchmarks for early hearing detection and intervention programs. These principles and guidelines are considered the standard of care today. Because positive results are referred to an audiologist or an Ear, Nose and Throat physician ( ENT ) for additional testing and evaluation, limiting the number of refers stemming from false positive results reduces the cost of a newborn screening program. In addition, false positive results can cause unnecessary emotional trauma for parents.

The 2007 JCIH Position Statement updated and expanded the definition of targeted hearing loss and recommended a specific protocol for babies admitted to the Neonatal Intensive Care Unit ( NICU ) for more than 5 days. Additionally, the document expressed increased awareness, not only of the need for diagnostic audiology evaluation for children diagnosed with hearing impairment at birth, but also for surveillance and hearing screening for children at risk of delayed onset and progressive hearing impairment during the first three years of life.

### *Newborn Hearing Screening Techniques*

The two traditional technologies used to screen newborns and infants for hearing impairment are auditory brainstem response and otoacoustic emissions.

*Auditory brainstem response ( ABR )*. Auditory brainstem response technology is the most accurate and comprehensive method for screening and diagnosing hearing impairment. Auditory brainstem response technology is based on detecting the brain's electric impulses resultant from a specific auditory stimulus. ABR screening devices, used for newborn hearing screening, detect and analyze the brainwave response resulting from audible click stimuli presented to the infant's ears. Automated Auditory Brainstem Response ( AABR ) devices were developed to automatically analyze the ABR waveform resulting from the auditory stimuli with computerized detection algorithms and statistical analysis. These devices can be used by any level of hospital personnel with a minimal amount of training and will deliver a clinically valid and accurate screen. The detection algorithms indicate a PASS or REFER result that requires no interpretation, thereby reducing staffing requirements, test times, and total hearing screening program costs. A REFER test result indicates that the patient should be referred to an Audiologist or ENT for further diagnostic evaluation.

*Otoacoustic emissions ( OAE )*. OAEs are sounds created by the active biomechanical processes within the sensory cells of the cochlea. They occur both spontaneously and in response to acoustic stimuli. OAE screening uses a probe placed in the ear canal to deliver auditory stimuli and to measure the response of the sensory cells with a sensitive microphone. OAE screening devices have technology that allows them to discriminate between randomly occurring OAEs, OAEs created by interfering room noise present in the test environment, and the OAEs that are a response to specific test stimuli. Automated OAE screening devices are capable of filtering non-specific OAEs in order to detect and analyze the OAEs that lead to an accurate screen of the infant's hearing. While a PASS test result indicates a proper functioning cochlea, a REFER test result indicates that the OAEs are absent or small compared to normal data. A REFER test result indicates that the patient should be referred to an Audiologist or ENT for further diagnostic evaluation. OAE technology is unable to detect hearing disorders affecting the neural pathways, such as auditory neuropathy. Estimates of the incidence rate of auditory neuropathy among hearing impaired newborns vary widely, but are thought to be in the range of 5% to 15%.

### *Newborn Hearing Screening Product Lines*

Our newborn hearing screening product lines consist of the ALGO, ABAer, AuDX, and Echo-Screen newborn hearing screeners. These hearing screening products utilize proprietary signal detection technologies to provide accurate and non-invasive hearing screening for newborns and are designed to detect hearing loss at 35 dB nHL or higher. Each of these devices is designed to generate a PASS or REFER result.

***ALGO 3 and 3i Newborn Hearing Screeners.*** These AABR devices deliver thousands of soft audible clicks to the newborn's ears through sound cables and disposable earphones connected to the instrument. Each click elicits an identifiable brain wave, which is detected by disposable electrodes placed on the head of the child, and analyzed by the screening device. These devices use our proprietary AABR signal detection algorithm.



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***ABaer Newborn Hearing Screener.*** The ABaer, which is a PC-based newborn hearing screening device, offers a combination of automatic ABR, OAE, and diagnostic ABR technologies in one system. The automatic ABR technology utilizes our patented Point Optimized Variance Ratio ( POVR ) signal detection algorithm developed by the House Ear Institute. Like our ALGO newborn hearing screeners, this device delivers thousands of soft audible clicks to the newborn s ears through sound cables and disposable earphones. Each click elicits an identifiable brain wave, which is detected by disposable electrodes placed on the head of the child, and analyzed by the screening device. The ABaer OAE software is the same technology used in our AuDX product and the diagnostic ABR software is the same technology used in our Navigator diagnostic hearing assessment product.

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***AuDX and Echo-Screen.*** Our AuDX and Echo-Screen products are hand-held OAE screening devices that can be used for newborn hearing screening, as well as for patients of all ages, from children through adults. These devices record and analyze OAEs generated by the cochlea through sound cables and disposable ear probes inserted into the patient's ear canal. OAE technology is unable to detect hearing disorders affecting the neural pathways, such as auditory neuropathy.

### ***Hearing Screening Supply Products***

For infection control, accuracy, and ease of use, the supply products used with our newborn hearing screening devices are designed as single-use, disposable products. Each screening supply product is designed for a specific hearing screening technology.

***ABR Screening Supply Kits.*** Each ABR screen is carried out with single-use earphones and electrodes, which are alcohol and latex-free. The adhesives used in these supply products are specially formulated for use on the sensitive skin of newborns. To meet the needs of our customers we offer a variety of packaging options.

***OAE Supply Products.*** Each OAE screen is carried out with single-use probe tips that are supplied in a variety of sizes and packaging options.

### ***Diagnostic Hearing Assessment***

#### ***Overview***

We design and manufacture a variety of products used to screen for or diagnose hearing loss, or to identify abnormalities affecting the peripheral and central auditory nervous systems. The technology used in most of these systems is either electrodiagnostic in nature or measures a response from the cochlea known as an otoacoustic emission.

Electrodiagnostic systems record electrical activity generated in the central nervous system. An electrodiagnostic testing device delivers acoustic stimuli to the ears while electrodes placed on the scalp record the brain's electrical response. The most common auditory test performed with electrodiagnostic equipment is the auditory brainstem response (ABR) test. This test, which records brainwaves that correspond to responses from the inner ear and brainstem, is used to screen for and define hearing loss characteristics, particularly for patients who cannot reliably respond to standard behavioral tests of hearing, either verbally or through motor response. A technician with minimal training can operate an instrument that performs an automated ABR screening test. More advanced ABR testing techniques that either define the nature of the hearing loss or that screen for other auditory abnormalities such as an acoustic tumor, require the expertise of a trained clinician, usually an audiologist or an ENT physician, an understanding of the technology being used, and the ability to interpret complex waveforms that represent the brain's electrical activity.

#### ***Diagnostic Hearing Assessment Product Lines***

Our diagnostic hearing assessment products consist of the Navigator Pro system, the Scout Sport portable diagnostic device, the HINT PRO, the AuDX PRO, the Cochlea-Scan, and the Centor.

***Navigator PRO.*** Our Navigator PRO for hearing assessment consists of a base system that is augmented by discrete software applications that are marketed as enhancements to the system. The Navigator Pro System is a PC-based, configurable device that utilizes evoked potentials, which are electrical signals recorded from the central nervous system that appear in response to repetitive stimuli, such as a clicking noise. The evoked potentials are used to record and display human physiological data associated with auditory and hearing-related disorders. The Navigator Pro System can be used for patients of all ages, from children to adults, including infants and geriatric patients. The device can be configured with additional proprietary software programs for various applications. These additional software programs include: Stacked ABR, CHAMP, MASTER, AEP, VEMP, BioMAP, and Scout.

***Scout SPORT.*** The Scout SPORT is a PC-based OAE system. The ultra portable Scout Sport can be carried from one computer to another to test in different locations. For office-based environments, the Scout Sport can be used with a dedicated notebook computer to create an independent portable system.

**HINT PRO.** Our *Hearing in Noise Test* application uses test sentences, procedures, and headphone norms developed by the House Ear Institute. The system features computerized administration, scoring, report generation, and data storage. The HINT measures the patient's ability to recognize and repeat short sentences presented in quiet or in noise. The speech and noise sources can be spatially separated to measure binaural directional hearing and spatial unmasking. The patient's sentence recognition threshold is measured in quiet and in three noise conditions.

**AuDX PRO.** The AuDX Pro is a hand-held OAE screening device with a large color display that can be used for patients of all ages, newborns through geriatrics. The AuDX records and analyzes OAEs generated by the cochlea through sound cables and disposable ear probes inserted into the patient's ear canal. A REFER test result indicates that the patient should be referred to an Audiologist or ENT for further diagnostic evaluation.

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***Cochlea-Scan.*** The Cochlea-scan is an easy to use handheld device to assess hearing loss. It utilizes Distortion Product Otoacoustic Emissions ( DPOAE ) technology, which allows the user to quantify hearing loss using physiologic measures instead of relying upon a patient's behavioral response.

***Centor.*** The Centor is a portable Audio-Evoked Potentials ( AEP ) product that records auditory evoked responses ( AERs ) in order to perform objective diagnoses as well as hearing-loss screening for adults and neonates. The system records AERs with standard or automatic protocols, including ABR, Middle Latency Audio-Evoked Potentials ( MLAEP ), ElectroCochleoGraphy ( EcochG ), Vestibular Evoked Myogenic Potentials ( VEMP ), as well as pure tone or vocal stimulation.

### ***Diagnostic Hearing Supply Products***

For infection control, accuracy, and ease of use, most supply products used with our diagnostic hearing devices and systems are designed as single-use, disposable products. Each screening supply product is designed for a specific diagnostic hearing technology, and is similar in nature to our previously described OAE supply products for use in newborn hearing screening.

### **Monitoring Systems for Neurology**

Our monitoring systems for Neurology represent a comprehensive line of products that are used by physicians, nurses and medical technologists to assist in the diagnosis and monitoring of neurological disorders of the central and peripheral nervous system, and as an aid in monitoring patients under sedation or post-operative care. Our product lines consist of the following:

***Electroencephalograph or EEG*** Equipment that monitors and visually displays the electrical activity generated by nerve cells in the brain for both diagnosis and monitoring of neurological disorders in the hospital, laboratory, office or patient's home;

***Polysomnography or PSG*** Equipment that measures a variety of respiratory and neurological functions to assist in the diagnosis and monitoring of sleep disorders, such as snoring and obstructive sleep apnea, a condition that causes a person to stop breathing intermittently during sleep;

***Electromyography or EMG*** Equipment that measures electrical activity in nerves and muscles, and the spinal cord; and

***Intra-operative Monitoring or IOM*** Products that assist surgeons in preserving the functional integrity of a patient's nervous system during and after complex surgical procedures.

### ***Diagnostic Electroencephalograph (EEG) Monitoring***

#### *Overview*

We design, manufacture, and market a full line of computerized instruments used to help diagnose the presence of seizure disorders and epilepsy, look for causes of confusion, evaluate head injuries, tumors, infections, degenerative diseases, and metabolic disturbances that affect the brain, and assist in surgical planning. This type of testing is also done to diagnose brain death in comatose patients. These systems and instruments work by detecting, amplifying, and recording the brain's electrical impulses (EEGs). Routine EEG recording is done by placing electrodes on a patient's scalp over various areas of the brain to record and detect patterns of activity and specific types of electrical events. EEG technologists perform the tests, and neurologists review and interpret the results.

Routine outpatient EEG testing is performed both in private physicians' offices and hospital EEG laboratories, providing physicians with a clinical assessment of a patient's condition. For patients with seizures that do not respond to conventional therapeutic approaches, long-term inpatient testing of EEGs and behavior is used to determine if surgical solutions are appropriate.

### ***Diagnostic Electroencephalograph (EEG) Monitoring Product Lines***

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Our diagnostic EEG monitoring product lines for neurology consist of devices operating with our proprietary software, augmented by signal amplifiers. These products are typically used in concert, as part of an EEG system by the neurology department of a hospital to assist in the diagnosis of assorted neurological conditions.

***Kortex; Ceegraph VISION; Coherence.*** Our computerized EEG Systems include a broad range of products, from software licenses and ambulatory monitoring systems to advanced laboratory systems with multiple capabilities for EEG, ICU monitoring, long-term epilepsy monitoring of up to 128 channels, and physician review stations with quantitative EEG analysis capabilities.

***Proprietary Signal Amplifiers.*** Our proprietary signal amplifiers function as the interface between the patient and the computer, and are also known as the headbox. The headbox connects disposable electrodes attached to the patient's head to our EEG monitoring systems. Our proprietary headbox products are sold for a wide variety of applications under the following brand names: Netlink EEG, Netlink LTM, Netlink Traveler, Traveler II, Trex, EEG32, EMU128, EMU40, and the Brain Monitor. Recent innovations in electronics technology and advanced internet-protocol data transmission enable certain of our amplifiers to record and transmit up to 32 channels of digital data using Ethernet communication.

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Several additional options are available to enhance our EEG products, including: a digital video option, which provides synchronized video recording of a patient's behavior while recording electrical activity from the brain; our patented SmartPack software option, which is an innovative data compression process that reduces the size of data files by as much as 60%, and our Universal Reader which is a physician's review station that permits fast and easy data analysis in a graphical format.

### ***Diagnostic Polysomnography (PSG) Monitoring***

#### *Overview*

Increasing public awareness of sleep disorders has made sleep medicine a rapidly growing specialty. The analysis of respiratory patterns, brain electrical activity and other physiological data has proven critical for the diagnosis and treatment of sleep-related diseases such as apnea, insomnia, and narcolepsy. A sleep study entails whole-night recordings of brain electrical activity, muscle movement, airflow, respiratory effort, oxygen levels, electrical activity of the heart ( ECG ), and other parameters. These recordings typically result in over 1,000 pages of data that are reviewed, analyzed, and scored by a technician, and summarized in a report for the physician. We market configured laboratory systems, portable systems, and ambulatory recorders for home monitoring.

#### ***Diagnostic Polysomnography (PSG) Monitoring Product Lines***

Our diagnostic PSG monitoring products can be used individually or as part of a networked system for overnight sleep studies to assist in the diagnosis of sleep disorders. These products include software licenses, ambulatory monitoring systems, and laboratory systems that combine multiple capabilities, including EEG monitoring, physician review stations, and quantitative EEG analysis capabilities.

***Sleepscan; Connex; SleepWorks; Coherence.*** Our diagnostic PSG systems capture and store all data digitally and provide time-saving features and software for acquiring and analyzing the data. The systems enable users to specify rules and personal preferences to be used during analysis, summarizing the results graphically and incorporating them in detailed reports. Our Sleepscan customized analysis includes color-coded sleep stages and flow loop analysis. The Coherence system utilizes a Pulse Transit Time device for the detection of respiratory events and arousals.

***Sleepscan Netlink.*** Our Sleepscan Netlink data acquisition system incorporates recent developments in superior amplifiers for sleep analysis. In addition to exceptional signal quality, the Netlink headbox includes a built-in oximeter, and allows the user to start and stop a study or perform electrode impedance testing either at the patient's bedside or from the monitoring room.

We also market a broad line of disposable products and accessories for the polysomnography laboratory. The Airflow Pressure Transducer uses pressure changes as an indicator of patient airflow levels, as contrasted to other monitoring devices that use temperature to indicate these levels. This product detects shallow breathing in situations where temperature related transducers might remain substantially unchanged. This method has been documented in industry publications to produce the signature waveform used in identifying a respiratory disorder known as Upper Airway Resistance Syndrome.

### ***Electromyography (EMG)***

#### *Overview*

An electromyogram (EMG) measures the electrical activity of muscles both at rest and during contraction. Measuring the electrical activity in muscles and nerves can help diagnose diseases that damage muscle tissue or nerves. An EMG is done to determine if there is any disease present that damages muscle tissue, nerves, or the junctions between nerve and muscle (neuromuscular junctions). An EMG can also be used to diagnose the cause of weakness, paralysis, and muscle twitching. It is also used as a primary diagnosis for carpal tunnel syndrome, which is the most frequently encountered peripheral compressive neuropathy.

#### ***Diagnostic Electromyography (EMG) Product Lines***

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**NeuroMAX.** A dedicated EMG device focused entirely on signal quality and clinical efficiency. The device gathers neurophysiological data that is saved to a fully customizable report, allowing physicians to take care of patients with the most informed advice.

**XCalibur.** An EMG system that uses advanced circuit design and digital signal processing to deliver clean signals, making the process of acquiring patient data reliable and quick. The system's software tools enrich data acquisition, reporting and review capabilities.

### ***Intra-operative Monitoring (IOM)***

#### *Overview*

Intra-operative monitoring is the use of electrophysiological methods such as EMG and EEG, to monitor the functional integrity of neural structures (brain, nerves, spinal cord) during surgery. The most common applications are in neurosurgery such as spinal surgery; some brain surgeries; ENT procedures and peripheral nerve surgery. IOM is used to localize neural structures and test the function of these structures for early detection of intra-operative injury, allowing for immediate corrective measures.

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### ***Intra-operative Monitoring Products***

***Protektor.*** An IOM system that provides medical professionals with all information necessary to make immediate and critical surgical decisions. The system combines flexibility with multi-modality allowing full coverage of intra-operative monitoring techniques.

### **Newborn Care**

#### ***Newborn Care Products***

Natus manufactures a wide variety of products used in the medical care of newborns. These product lines include products to diagnose and treat newborn brain injury, as well as a line of phototherapy lights to treat newborn jaundice. The Company also sells a variety of newborn care products to meet the needs of clinicians in the nursery and Neonatal Intensive Care Unit.

#### ***Newborn Brain Injury***

##### ***Overview***

For many years, newborn infants admitted to the neonatal intensive care unit of a hospital have routinely been monitored for heart activity, temperature, respiration, oxygen saturation, and blood pressure. Only recently has it also been considered important to monitor brain activity using continuous electroencephalography ( EEG ). A cerebral function monitor, utilizing amplitude-integrated EEGs ( aEEGs ), is a device for monitoring background neurological activity.

##### ***Neurological Assessment and Treatment Options***

Early diagnosis of brain injury in newborns, when combined with early intervention, has been shown to reduce the severity of these brain injuries and in some cases, save the patient's life. These brain injuries, which can occur in as many as three out of every 1,000 newborns, are caused by conditions such as hypoxic ischemic encephalopathy ( HIE ), subclinical seizures, or neurological disorders. Diagnosing these conditions shortly after birth is imperative, as patients who undergo therapy within six hours after birth show a greater potential for improved outcomes.

Clinical studies have also shown that recent advancements in two primary technologies can have a marked and positive impact upon newborn brain injury. These technologies are amplitude-integrated EEG and servo-controlled patient cooling.

#### ***Newborn Brain Injury Product Line***

***Olympic CFM-6000 System.*** The Cerebral Function Monitor ( CFM ) provides the Neurologist with the technology to diagnose neurological disorders or brain injury in the newborn. The device continuously monitors and records brain activity, aiding in the detection and treatment of HIE and seizures. The device also monitors the effects of drugs and other therapies on brain activity and improves the accuracy of newborn neurological assessments. The Olympic CFM-6000 helps determine the need for further neurological examination or transport to a tertiary-care center. The CFM is used with electrodes attached to the head of the newborn to acquire an aEEG signal that is then filtered, compressed, and displayed graphically on the device or as a hardcopy printout.

***Olympic Cool-Cap System.*** The Olympic Cool-Cap is the only FDA approved device for administering selective head cooling as a treatment for moderate to severe HIE. A four-year clinical trial for the Cool-Cap was completed in 2006, and the FDA gave approval for the product in December 2006. The clinical trial validated the benefit of direct brain cooling in reducing the severity of brain injury resulting from newborn HIE. Both the device and the proprietary software conform to the clinical trial protocol and are designed to assist the clinician in safely administering the treatment, thereby preventing or significantly reducing the severity of neurological injury associated with HIE.

***Newborn Brain Injury Supply Products.*** In addition to disposable electrodes used to perform each aEEG test using the CFM-6000, the Olympic Cool-Cap brain cooling system uses a single-patient, disposable, cooling cap to continuously circulate sterile water to the patient during the 72-hour treatment period.

#### ***Jaundice Management Products***



*Overview*

The American Academy of Pediatrics estimates that each year 60% of the approximately four million newborns in the U.S. become jaundiced. According to the Journal of the American Medical Association, neonatal jaundice is the single largest cause for hospital readmission of newborns in the U.S., and accounts for 50% of readmissions. Because of the serious consequences of hyperbilirubinemia, the American Academy of Pediatrics recommends that all newborns be closely monitored for jaundice and has called for the physician to determine the presence or absence of an abnormal rate of hemolysis to establish the appropriate treatment for the newborn.

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In 2004, the American Academy of Pediatrics issued new guidelines for the treatment of jaundice in newborns. The guidelines recommend phototherapy as the standard of care for the treatment of hyperbilirubinemia in infants born at 35 weeks or more of gestation. The guidelines further highlight the need for intense phototherapy, and specifically recommend the use of the blue light treatment incorporated into our neoBLUE products.

We currently offer the following products that meet guidelines of the American Academy of Pediatrics for the treatment of newborn jaundice:

**neoBLUE Product Family.** This product line consists of our neoBLUE, neoBLUE Mini, and neoBLUE Cozy devices, which utilize Light Emitting Diodes ( LEDs ) to generate a high-intensity, narrow spectrum of blue light that is clinically proven to be most effective in the treatment of newborn jaundice. The neoBLUE phototherapy devices emit significantly less ultraviolet light and heat than conventional phototherapy devices, reducing the risk of skin damage and dehydration for infants undergoing treatment. Because of the high intensity of these lights, the treatment time associated with phototherapy is reduced.

**Bili-Lite Product Family.** These devices utilize fluorescent light bulbs for the treatment of hyperbilirubinemia. The Bili-Bassinet provides intensive phototherapy from both under and over the baby for maximum surface area coverage. The Bili-Lite pad is a product designed for home-based phototherapy; because of its design, it does not require the use of eye shields, making it easier for parents to use.

### ***Other Newborn Care Product Lines***

**Medical Devices.** These products include devices such as: photometers, radiometers, patient warming lamps, pediatric scales, blanket warming cabinets, exam lights, oxygen hoods, and our newborn circumstraint.

**Disposable Supplies.** These products include disposable supplies such as: neonatal noise attenuators, phototherapy eye masks, restraining boards, and x-ray shields for newborn gonads.

**Newborn Screening Data Management Product Line.** Our suite of newborn screening data management products consists of proprietary software that collects, tracks, manages and reports newborn screening data to regional government health laboratories and national disease control centers. While all states have laws and/or regulations requiring newborn screening for metabolic disorders, the laws and regulations vary widely in the extent of screening required. Recently some states have begun using tandem mass spectrometry in their newborn metabolic screening programs, which has greatly increased the number of treatable disorders that can be detected. Revenue from installation and upgrades of our newborn screening data management systems is classified as devices and systems revenue, as more fully described below. Revenue from maintenance contracts on these systems is classified as supplies and services revenue, as more fully described below.

## **Segment and Geographic Information**

We operate in one reportable segment in which we provide healthcare products used for the screening, detection, treatment, monitoring and tracking of common medical ailments such as hearing impairment, neurological dysfunction, epilepsy, sleep disorders, and newborn care, including jaundice, brain injury, and metabolic testing. We develop, manufacture, and market advanced neurodiagnostic and newborn care products to healthcare professionals in over 80 countries. Our product offerings include computerized neurodiagnostic systems for audiology, neurology, polysomnography, and neonatology, as well as newborn care products such as hearing screening systems, phototherapy devices for the treatment of newborn jaundice, head-cooling products for the treatment of brain injury in newborns, and software systems for managing and tracking disorders and diseases for public health laboratories.

Our end-user customer base includes hospitals, clinics, laboratories, physicians, nurses, audiologists, and governmental agencies. Most of our international sales are to distributors, who in turn, resell our products to end users or sub-distributors.

Information regarding our sales and long-lived assets in the U.S. and in countries outside the U.S. is contained in *Note 16 Segment, Customer and Geographic Information* of our consolidated financial statements included in this report and is incorporated in this section by this reference.

### ***Revenue by Product Family and Product Category***

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For the years ended December 31, 2007, 2006 and 2005, revenue from our four product families as a percent of total revenue was approximately as follows:

	Year Ended December 31,		
	2007	2006	2005
Hearing	53%	61%	77%
Monitoring Systems for Neurology	14%	19%	%
Newborn Care	28%	15%	20%
Other	5%	5%	3%
Total	100%	100%	100%

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We expect that with the acquisition of Xltek, which was effective November 29, 2007, revenue from our Monitoring Systems for Neurology product family will contribute to a greater portion of total revenue in the future.

We also look at revenue as either being generated from sales of Devices and Systems, which are generally non-recurring, or related Supplies and Services, which are generally recurring. The products that are attributable to these categories are described above. Revenue from Devices and Systems, and Supplies and Services, as a percent of total revenue for the years ending December 31, 2007, 2006 and 2005 is as follows:

	Year Ended December 31,		
	2007	2006	2005
Devices and Systems	62%	57%	45%
Supplies and Services	37%	41%	54%
Other	1%	2%	1%

Total 100% 100% 100%

In 2007, 2006 and 2005, sales to no single end-user customer comprised more than 10% of our revenue, and revenue from services was less than 10% of our revenue.

**Backlog**

As of December 31, 2007, the Company's backlog was approximately \$4.4 million, compared to \$2.9 million at December 31, 2006 and an immaterial amount at December 31, 2005. We anticipate that we will complete all of the backlog orders by the fourth quarter of 2008.

**Marketing and Sales**

***Marketing***

Our marketing strategy differentiates our products by their level of quality, performance, and customer benefit. We educate customers and potential customers worldwide about our products through several traditional methods, including, but not limited to:

Trade conference exhibits;

Direct presentations to healthcare professionals;

Publications in professional journals and trade magazines;

The Internet via our website, [www.natus.com](http://www.natus.com);

Print and direct mail advertising campaigns; and

Sponsorship of and participation in clinical education seminars.

Educational efforts directed at government agencies and key physicians and clinicians about the benefits of universal screening in terms of patient outcomes and long-term treatment costs are a key element of our marketing strategy.

***Domestic Sales***

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We sell our products in the United States primarily through a direct sales organization. This direct sales organization is a significant benefit to the Company, we believe, allowing us to maintain a higher level of customer service and satisfaction than would otherwise be possible by another distribution method. Revenue from our direct sales channels as a percent of total revenue was 57%, 64% and 84% in 2007, 2006 and 2005, respectively. The reduction of revenue sold through our direct sales channels as a percent of total revenue in 2007 and 2006 compared to 2005 resulted from an increase in sales of our line of diagnostic hearing products, which are sold through distributors. We gained this product line through our acquisition of Bio-logic in January 2006. We also sell certain products under private label arrangements. Domestic revenue resulting from sales through both of these non-direct sales channels was 10% of total revenue in 2007, 11% of total revenue in 2006 and an immaterial percentage in 2005.

### ***International Sales***

We sell our products outside the U.S. primarily through a distributor sales channel, which consists of distributors selling Natus products into more than 80 countries as of December 31, 2007. We sell products to our distributors under substantially the same terms as sales through our direct sales channels. Terms of sales to international distributors are EXW, reflecting that goods are shipped ex works, in which title and risk of loss are assumed by the distributor at the shipping point. Distributors are generally given exclusive rights in their territories to purchase products from Natus and resell to end users or sub-distributors. Our distributors typically perform marketing, sales, and technical support functions in their respective markets. Each distributor may sell Natus products to their customer directly, via other distributors or resellers, or both. We actively train our distributors in product marketing, selling, and technical service techniques.

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Through our acquisition of Deltamed in September 2006, we now sell some of our products in France and Germany through a direct sales organization. We previously had direct sales organizations in Japan and the United Kingdom ( U.K. ). However, in 2004 we ceased selling through a direct sales force in Japan and began to sell through a distributor, and in February 2006 we ceased selling through a direct sales force in the U.K. and began to sell through a distributor.

Revenue from international sales was approximately 33%, 29% and 36% of our total revenue in 2007, 2006 and 2005, respectively.

### ***Seasonality in Revenue***

We experience seasonality in our revenue. Our revenue typically drops from our fourth quarter to our first quarter. This seasonality results from the purchasing habits of our hospital-based customers, whose purchases are often governed by calendar year budgets, and the manner in which our direct sales force is compensated, as their compensation is based on annual sales plans that are tied to our December year end.

### ***Group Purchasing Organizations***

More than 90% of the hospitals in the U.S. are members of group purchasing organizations ( GPO s), which negotiate volume purchase prices for member hospitals, group practices, and other clinics. Direct purchases by members of group purchasing organizations accounted for approximately 35%, 31% and 28% of our revenue in 2007, 2006 and 2005, respectively. Direct purchases by members of one GPO, Novation, accounted for approximately 9%, 12% and 15% of our revenue in 2007, 2006 and 2005, respectively. Our revenue recognition policies related to sales to GPO members are described in Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations, contained in this report.

### ***Third-Party Reimbursement***

In the U.S., health care providers generally rely on third-party payors, including private health insurance plans, federal Medicare, state Medicaid, and managed care organizations, to reimburse all or part of the cost of the procedures they perform. Third-party payors can affect the pricing or the relative attractiveness of our products by regulating the maximum amount of reimbursement these payors provide for services. In general, reimbursement for newborn screening is included in the lump-sum payment for the newborn s birth and hospitalization. For this reason, we are not able to measure a reimbursement success rate for our screening products.

### ***Customer Service and Support***

We provide a one-year warranty on all medical device products. We also sell extended service agreements on our medical device products. Service, repair, and calibration services for our domestic customers is provided by Company-owned service centers and our employee field service specialists. Service for our international customers is provided by a combination of our Company-owned authorized service centers and third-party vendors on a contract basis.

### ***Manufacturing***

Other companies manufacture a significant portion of the components used in our products; however, we perform final assembly, testing, and packaging of most of the devices ourselves to control quality and manufacturing efficiency. We also use contract vendors to manufacture some of our disposable supply and medical device products. We perform regular quality audits of these vendors.

We purchase materials and components from qualified suppliers that are subject to our quality specifications and inspections. We conduct quality audits of our key suppliers, several of which are experienced in the supply of components to manufacturers of finished medical devices, or supplies for use with medical devices. Most of our purchased components are available from more than one supplier.

Our manufacturing, service, and repair facilities are subject to periodic inspection by federal, state, and foreign regulatory authorities. Our quality assurance system is subject to regulation by the FDA and other state government agencies. We are required to conduct our product design, testing, manufacturing, and control activities in conformance with the FDA s quality system regulations and to maintain our documentation of these activities in a prescribed manner. In addition, our production facilities have received ISO 13485 certification. ISO 13485 certification standards for quality operations have been developed to ensure that medical device companies meet the standards of quality on a worldwide basis. We have also received the EC Certificate pursuant to the European Union Medical Device Directive 93/42/EEC, which allowed us to place a CE mark on our products after assembling appropriate documentation.

**Research and Development**

We are committed to introducing new products and supporting current product offerings in our markets through a combination of internal as well as external efforts that are consistent with our corporate strategy.

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*Internal product development capabilities.* We believe that product development capabilities are essential to provide our customers with new product offerings. We plan to leverage our core technologies by introducing product line extensions as well as new product offerings.

*Partnerships that complement our expertise.* We continue to seek strategic partners in order to develop products that may not otherwise be available to us. By taking advantage of our core competencies, we believe that we can bring products to market in an efficient manner, and leverage our distribution channels.

*New opportunities through technology acquisition.* We continue to evaluate new, emerging, and complementary technologies in order to identify new product opportunities. With our knowledge of our current markets we believe that we can effectively develop technologies into successful new products.

Our research and development expenses were \$15.6 million or 13.2% of total revenue in 2007, \$10.6 million or 11.8% of total revenue in 2006 and \$4.3 million or 10.0% of total revenue in 2005.

## **Proprietary Rights**

We protect our intellectual property through a combination of patent, copyright, trade secret, and trademark laws. We attempt to protect our intellectual property rights by filing patent applications for new features and products we develop. We enter into confidentiality or license agreements with our employees, consultants, and corporate partners, and seek to control access to our intellectual property, distribution channels, documentation, and other proprietary information. However, we believe that these measures afford only limited protection.

The intellectual rights to some of the original patents for technology incorporated into our products are now in the public domain. However, we do not consider these patents, or any currently viable patent or related group of patents to be of such importance that their expiration or termination would materially affect our business.

We capitalize the cost of purchased technology and intellectual property, as well as certain costs incurred in obtaining patent rights, and amortize these costs over the estimated economic lives of the related assets.

## **Competition**

We sell our products in competitive and rapidly evolving markets. We face competition from other companies in all of our product lines. Our competitors range from small, privately-held companies to multinational corporations and their product offerings vary in scope and breadth. We do not believe that any single competitor is dominant in any of our product lines.

We derive a significant portion of our revenue from the sale of disposable supplies that are used with our medical devices. In the U.S., we sell our supply products in a mature market. Because these products can generate high margins, we expect that our products, particularly our hearing screening supply products, could face increasing competition, including competitors offering lower prices, which could have an adverse affect on our revenue and margins.

We believe the principal factors that will draw clinicians and other buyers to our products, include:

Level of specificity, sensitivity, and reliability of the product;

Time required to obtain results with the product, such as to test for or treat a clinical condition;

Relative ease of use of the product;

Depth and breadth of the products features;



Quality of customer support for the product;

Frequency of product updates;

Extent of third-party reimbursement of the cost of the product or procedure;

Extent to which the products conform to standard of care guidelines; and

Price of the product.

We believe that our primary competitive strength relates to the functionality and reliability of our products. Different competitors may have competitive advantages in one or more of the categories listed above and they may be able to devote greater resources to the development, promotion, and sale of their products.

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### **Government Regulation**

#### ***FDA s Premarket Clearance and Approval Requirements***

Unless an exemption applies, the medical devices we sell, with the exception of some disposable products in our newborn care products, must first receive one of the following types of FDA premarket review authorizations under the Food, Drug, and Cosmetics Act, as amended:

Clearance via Section 510(k); or

Premarket approval via Section 515 if the FDA has determined that the medical device in question poses a greater risk of injury. The FDA s 510(k) clearance process usually takes from three to 12 months, but can take longer. The process of obtaining premarket approval via Section 515 is much more costly, lengthy, and uncertain. Premarket approval generally takes from one to three years, but can take longer. We cannot be sure that the FDA will ever grant either 510(k) clearance or premarket approval for any product we propose to market.

The FDA decides whether a device must undergo either the 510(k) clearance or premarket approval process based upon statutory criteria. These criteria include the level of risk that the Agency perceives to be associated with the device and a determination of whether the product is a type of device that is substantially equivalent to devices that are already legally marketed. The FDA places devices deemed to pose relatively less risk in either class I or class II, which requires the manufacturer to submit a premarket notification requesting 510(k) clearance, unless an exemption applies. The premarket notification under Section 510(k) must demonstrate that the proposed device is substantially equivalent in intended use and in safety and effectiveness to a previously cleared 510(k) device or a device that was in commercial distribution before May 28, 1976 for which the FDA has not yet called for the submission of premarket approval applications.

The FDA places devices deemed to pose the greatest risk, such as life-sustaining, life-supporting or implantable devices, or devices deemed to be not substantially equivalent to a predicate device, in its Class III classification. The FDA requires these devices to undergo the premarket approval process via Section 515 in which the manufacturer must prove the safety and effectiveness of the device. A premarket approval application must provide extensive pre-clinical and clinical trial data.

The FDA may require results of clinical trials in support of a 510(k) submission and generally requires clinical trial results for a premarket approval application. In order to conduct a clinical trial on a significant-risk device, the FDA requires manufacturers to apply for and obtain, in advance, an investigational-device exemption. The investigational-device exemption application must be supported by appropriate data, such as animal and laboratory testing results. If the FDA and the Institutional Review Boards at the clinical trial sites approve the investigational-device exemption application for a significant-risk device, the manufacturer may begin the clinical trial. An investigational-device exemption approval provides for a specified clinical protocol, including the number of patients and study sites. If the manufacturer deems the product a non-significant risk device, the product will be eligible for more abbreviated investigational-device exemption requirements. If the Institutional Review Boards at the clinical trial sites concur with the non-significant risk determination, the manufacturer may begin the clinical trial.

We received approval for our Olympic Cool-Cap product as a Class III device from the FDA through the premarket approval process. Most of our other products in our newborn hearing screening, diagnostic hearing, EEG monitoring, polysomnography, and newborn care product lines have been approved by the FDA as Class II devices. Some of our disposable products and newborn care products, such as our neonatal headshields and oxygen delivery systems, have received FDA approval as Class I devices.

#### ***FDA Regulation***

Numerous FDA regulatory requirements apply to our marketed devices. These requirements include:

FDA quality system regulations which require manufacturers to create, implement, and follow design, testing, control, documentation, and other quality assurance procedures;

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Medical device reporting regulations, which require that manufacturers report to the FDA certain types of adverse and other events involving their products; and

FDA general prohibitions against promoting products for unapproved uses.

Class II and Class III devices may also be subject to special controls applied to them, such as performance standards, post-market surveillance, patient registries, and FDA guidelines that may not apply to Class I devices. We believe we are in compliance with the applicable FDA guidelines, but we could be required to change our compliance activities or be subject to other special controls if the FDA changes its existing regulations or adopts new requirements.

We are subject to inspection and market surveillance by the FDA to determine compliance with regulatory requirements. If the FDA finds that we have failed to adequately comply, the Agency can institute a wide variety of enforcement actions, ranging from a public warning letter to more severe sanctions such as:

Fines, injunctions, and civil penalties;

Recall or seizure of our products;

Issuance of public notices or warnings;

Imposition of operating restrictions, partial suspension, or total shutdown of production;

Refusal of our requests for 510(k) clearance or pre-market approval of new products;

Withdrawal of 510(k) clearance or pre-market approval already granted; or

Criminal prosecution.

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The FDA also has the authority to require us to repair, replace, or refund the cost of any medical device manufactured or distributed by us.

**Other U.S. Regulations**

We also must comply with numerous additional federal, state, and local laws relating to matters such as safe working conditions, manufacturing practices, environmental protection, biohazards, fire hazard control, and hazardous substance disposal. We believe we are currently in compliance with applicable safety, quality, environmental-protection, biohazard, and hazardous-substance-disposal regulations.

**Foreign Regulation**

In the foreign countries in which we sell or plan to sell our FDA-regulated products, these products are also regulated as medical devices, and are subject to regulatory requirements by foreign governmental agencies similar to those of the FDA. Our manufacturing facilities are audited and have been certified to be ISO9001/EN46001 compliant, which allows us to sell our products in Europe. Our manufacturing facilities are subject to CE Mark and ISO 9001 inspection by TÜV Rheinland. We plan to seek approval to sell our products in additional countries. The time and cost required to obtain market authorization from other countries and the requirements for licensing a product in another country may differ significantly from FDA requirements.

**Employees**

On December 31, 2007, we had approximately 435 full time employees worldwide. None of our employees are represented by a labor union. We have not experienced any work stoppages and consider our relations with our employees to be good.

**Executive Officers**

The following table lists our executive officers and their ages as of March 1, 2008:

<b>Name</b>	<b>Age</b>	<b>Position(s)</b>
James B. Hawkins	52	President, Chief Executive Officer, and Director
Steven J. Murphy	56	Vice President Finance and Chief Financial Officer
William L. Mince	56	Vice President Operations
Kenneth M. Traverso	47	Vice President Marketing and Sales
D. Christopher Chung, M.D.	44	Vice President Medical Affairs, R&D, and Engineering

*James B. Hawkins* has served as President and Chief Executive Officer, and as a member of the Board of Directors, since joining Natus in April 2004. Mr. Hawkins has over 25 years of combined medical device and financial management experience. Prior to joining Natus, he was President and Chief Executive Officer of Nasdaq-Traded Invivo Corporation for 19 years. Invivo Corporation, a maker of multi-parameter vital sign monitoring equipment used in hospitals, was acquired in early 2004 by Intermagnetics General Corporation. He earned a Bachelor of Commerce degree, specialized in Management from Santa Clara University and a Masters of Business Administration Finance degree from San Francisco State University. Mr. Hawkins is a Director of Iridex Corp.

*Steven J. Murphy* has served as Chief Financial Officer since February 2006, Vice President Finance since June 2003, and joined Natus in September 2002 as Director of Finance. From February 2002 through September 2002, Mr. Murphy was interim Controller at Travel Nurse International, a temporary staffing firm that was acquired by Medical Staffing Network in December 2002. From October 1998 through January 2002, Mr. Murphy was Controller of AdvisorTech Corporation, an international software development company providing IT-based solutions in the field of investments, where he was responsible for financial reporting of domestic, Asian and European operations with significant reporting responsibilities to the board of directors and investor groups. From 1996 to 1998 he was Vice President Finance of RWS Group, LLC, an international service company providing management of language-related projects. Mr. Murphy holds a Bachelor of Science degree in Business Administration from California State University, Chico. Mr. Murphy is a certified public accountant.

*William L. Mince* has served as our Vice President, North American Operations since September 2007 and joined Natus as Vice President Operations in October 2002. From November 2000 to September 2002, Mr. Mince served as President and Founder of My Own Jukebox, an Internet retail company. From July 1998 to October 2000, Mr. Mince was a consultant with the majority of his time spent as Senior Vice President Network Solutions for Premier Retail Network, a media broadcasting company. From July 1997 to June 1998, Mr. Mince served as President and Chief Operating Officer of Ophthalmic Imaging Systems, a publicly-held medical device company. From July 1994 to June 1997, Mr. Mince was Vice President Operations with Premier Retail Network. From May 1988 to June 1994, Mr. Mince was Director of Operations

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for Nellcor, a medical device company. Mr. Mince holds a Bachelor of Science degree in Business Administration from the University of Redlands and a Masters of Business Administration degree from National University.

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*Kenneth M. Traverso* has served as our Vice President Marketing and Sales since April 2002. From September 2000 to April 2002, he served as our Vice President Sales. From October 1999 to July 2000, Mr. Traverso served as President of DinnerNow.com Inc., an internet aggregator for the restaurant industry. From January 1998 to September 1999, Mr. Traverso served as Vice President Sales, Western Region of Alere Medical, an outpatient chronic disease management company. From May 1995 to January 1998, Mr. Traverso served as Vice President Marketing and Sales of AbTox, Inc., a low temperature sterilization company. From August 1990 to May 1995, Mr. Traverso served in various capacities at Natus, including Vice President Sales. From September 1984 to July 1990 Mr. Traverso served various positions at Nellcor, a medical device company, including Regional Sales Manager, Western Region. Mr. Traverso holds a Bachelor of Science degree in Administration & Marketing from San Francisco State University.

*D. Christopher Chung, M.D.*, has served as our Vice President R&D and Engineering since June 2003, and has served as our Vice President Medical Affairs since February 2003. Dr. Chung also served as our Medical Director from October 2000 to February 2003. From August 2000 to December 2007, Dr. Chung also served as a Pediatric Hospitalist at the California Pacific Medical Center in San Francisco. Dr. Chung has been a member of the Medical Advisory Board of eHealth Global Technologies, Inc. since April 2007 and has served as a member of their Board of Directors since November 2007. From June 1997 to June 2000, Dr. Chung trained as a pediatric resident at Boston Children's Hospital and Harvard Medical School. From May 1986 to July 1993, Dr. Chung worked as an Engineer at Nellcor, a medical device company. Dr. Chung holds a Bachelor of Arts degree in Computer Mathematics from the University of Pennsylvania and a Doctor of Medicine degree from the Medical College of Pennsylvania-Hahnemann University School of Medicine. He is a licensed physician and is a Fellow of the American Academy of Pediatrics.

## **Other Information**

We maintain corporate offices at 1501 Industrial Road, San Carlos, California 94070. Our telephone number is (650) 802-0400. We maintain a World Wide Web site at [www.natus.com](http://www.natus.com). References to the Company's website address do not constitute incorporation by reference of the information contained on the website, and the information contained on the website is not part of this document.

We make available, free of charge at our corporate website, copies of our Annual Reports on Form 10-K, Quarterly reports on Form 10-Q, Current Reports on Form 8-K, Proxy Statements, and all amendments to these reports, as soon as reasonably practicable after such material is electronically filed with or furnished to the Securities and Exchange Commission pursuant to Section 13(a) or 15(d) of the Securities Exchange Act. We also show detail about stock trading by corporate insiders by providing access to SEC Forms 3, 4 and 5. This information may also be obtained from the SEC's on-line database, which is located at [www.sec.gov](http://www.sec.gov). Our common stock is traded on the Nasdaq Stock Market under the symbol **BABY**.

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### **ITEM 11. EXECUTIVE COMPENSATION.**

#### **COMPENSATION DISCUSSION AND ANALYSIS**

##### **General**

Our executive compensation program is designed to attract, as needed, individuals with the skills necessary for us to achieve our business plan, to reward those individuals fairly over time, to retain those individuals who continue to perform at or above the levels that we expect and to closely align the compensation of those individuals with the performance of our company on both a short-term and long-term basis.

##### **Our Business and Our Compensation Philosophy**

We believe that opportunities exist for us to increase stockholder value by increasing the revenue base, and by doing so the income earning capacity, of our company. We seek growth in two ways, through organic growth involving, primarily, the introduction of existing products into new markets and the internal development of new products, and through acquisitions of complementary products and businesses. Our business plans challenge our executives to seek growth through both of these means, and we expect over time to achieve a higher level of growth than could be achieved through either of them alone. Further, we expect our business, including the businesses that we acquire, to be operated efficiently so that earnings can grow as we increase revenue.

Pursuit of this business model is demanding on our executives. They must implement efforts to enhance sales opportunities of existing products, oversee effective and efficient new product development and enhancements, successfully identify and complete the acquisition of complementary products and businesses and integrate these operations with our existing businesses, as well as conduct our business in an efficient manner.

In consideration of these factors, the primary objectives of our executive compensation are:

*Retain Qualified Executive Talent.* We have increased our revenue nearly four-fold from 2003 to 2007 and during this period completed five acquisitions of companies with principal offices in four different countries, and believe that maintaining continuity within our executive team has contributed significantly to our ability to achieve this growth. Our business is competitive and our headquarters are in an area where there is significant competition for executive talent. In light of these factors, a key objective of our compensation is to allow us to retain qualified executives. We believe that our ability to keep our senior executive team intact over the past four years reflects some measure of success of our compensation programs.

*Attract Qualified Executives.* While we have had no significant changes in our executive staff over the last four years, we understand that we may find it in our interests to, or may be required to, add new individuals to our executive team. This may especially be the case if we continue to grow our business and thereby increase the level of skills needed to manage it and the size of the management team charged with doing so. For us to be appropriately positioned to attract new talent as needed, we must be prepared to, and perceived as an employer that is willing to, offer competitive compensation.

*Link Compensation to Achievement of Our Business Objectives.* We believe that the single performance factor most capable of increasing stockholder value for the company is growth in earnings. As a result, we believe that a significant portion of the current period cash compensation that our executives are eligible to receive should be tied to attainment of the earnings target incorporated into our annual business plan, and that if we achieve our plans our executives should be rewarded commensurately.

*Provide Direct Incentives for the Enhancement of Stockholder Value Over the Long Term.* The effectiveness of our management in operating our business has a strong influence on the value of our common stock over time. We believe that our executives should be positioned to share, with our stockholders, in the gains and losses from changes in the value of our common stock over time and that this form of compensation will further motivate our executives to seek to increase stockholder value.

##### **Elements of Compensation**

Our executive officers' compensation currently has two primary elements of compensation—cash compensation, in the form of salary and annual incentive awards, and equity awards, in the form of stock options and restricted stock grants. In addition, we provide our executive officers with benefits that are available generally to all salaried employees.

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We believe that we would impair our ability to retain our executives or, as required, attract new executives if we did not offer a competitive salary. As such, our goal is to provide salaries that are sufficient to make us reasonably confident of our ability to retain our executive team without overpaying. We further believe that a substantial portion of the cash compensation that our executives are eligible to receive should be directly tied to corporate performance. We believe that our annual business plans, which are the basis for our annual incentive plans, represent reasonably challenging targets, the achievement of which should position us to increase stockholder value. For instance, our non-GAAP income before tax, which corresponds closely to pre-tax profit in our business plan, grew 35% in 2007 over 2006, but this did not meet the threshold for payment under our incentive plan and our executive team did not



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receive an incentive award for 2007. Equity awards are designed both for the provision of a competitive compensation package and for the purpose of providing a further incentive to our executives to increase stockholder value. We explain below with greater specificity how the Compensation Committee determines the amount paid or granted under such element.

In establishing compensation, we take into account the compensation that is payable by companies that we believe to be our competitors and by other companies with which we believe we generally compete for executives. To this end, our Compensation Committee works with management and an outside compensation consultant to define the specific criteria used to identify appropriate market comparisons for establishing compensation levels and the mix of salary, incentive compensation and equity compensation. When determining our peer companies, we focused on identifying companies with whom Natus competes directly for customers and employees, as well as other medical device companies, and in particular focus on companies headquartered in the San Francisco Bay Area. In addition, we selected companies that are generally within our size, limiting the peer group to companies whose annual revenue was within a range of approximately .5x to 2.0x our revenue run rate at the end of 2007. The peer companies that we reviewed are: Abaxis; Analogic; Aspect Medical Systems; Cardiac Science; Cholestech; Digirad; Possis Medical; Sonosite; Thoratec; Vital Signs; and Zoll Medical. For the purpose of establishing the components of compensation as described below relative to the peer group's compensation, our advisor evaluated compensation for the most recently completed fiscal year for which the respective peer group companies have provided compensation information in their proxy materials.

In determining the compensation of each of our executive officers, other than the Chief Executive Officer, our Compensation Committee considers the recommendations of the Chief Executive Officer.

We view the cash and equity elements of compensation as distinct. We think that each of these main components must be perceived by our executives as competitive with the corresponding compensation element paid by our peer companies. Within our cash compensation, the salary and incentive payments are linked in terms of benchmarking. We structure our salaries to be approximately the median of our peer companies and for 2007 and 2008 our incentive plan was targeted so that cash bonus payments at the target level would provide aggregate cash compensation (that is, salary plus bonus) at approximately the median level of our peer companies and aggregate cash payments at the 75<sup>th</sup> percentile of the peer group if incentive payments were paid at the highest level.

We used the median level as our benchmark for salaries and aggregate cash consideration, as we thought this would be sufficient to achieve our retention goals. We used the 75<sup>th</sup> percentile as the target for the high end of aggregate cash compensation because we adopt business plans that are a challenge for us to achieve, and we believe that if our executives exceed the demanding targets in these plans they should be eligible to receive higher levels of compensation. This being the case, we have not undertaken to determine the extent to which our performance targets are more or less difficult to achieve than those of our peer group because we did not think that it would be feasible to do so.

We view our compensation decisions as an exercise in paying competitive compensation, with desired performance goals, on an annual basis. Our cash compensation is not tied to performance beyond one year. Our equity awards vest over a period of time and as such are impacted by the value of our common stock over the life of the option or the vesting period of the restricted stock, as the case may be. We do not take account of prior wealth accumulation by our executives from the receipt of cash on exercise or vesting of equity awards as we do not believe these prior period returns provide a significant motivation or retention benefit in the current period. Further, we do not set the compensation of our executives at any multiple or ratio to the compensation of other executives or employees. Our Compensation Committee has not adopted any formal or informal policies or guidelines for allocating compensation between long-term and immediate compensation, between cash and non-cash compensation, or among different forms of non-cash compensation, other than as described below for the manner in which we make stock option and restricted stock awards to executives.

Our Compensation Committee's current intent is to perform on a regular basis a strategic review of our executive officers' overall compensation packages to determine whether they provide adequate incentives and motivation and whether they adequately compensate our executive officers relative to comparable officers in our peer group companies.

### **Cash Compensation Element**

As noted above, we seek to pay base salaries that are at the median level of our peer group. Annual increases in base salary are determined on an individual basis, primarily based on market data. We may also adjust salary up or down if we think such a change is merited on the basis of the officer's personal performance, but did not make any such adjustments for 2007 or 2008. In 2007, the executive officers, other than the Chief Executive Officer of the Company, received salary increases ranging from 7% to 13% over their salaries for 2006.

Our 2007 incentive plan was, and our 2008 incentive plan is, based on the attainment of the pre-tax earnings measure that is contained in the business plan approved by our board of directors for the operation of our business for the full year. We choose this single metric because we believe that over time our earnings are the key driver of stockholder returns. We chose pre-tax earnings in particular as various factors, some of

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which we have limited ability to control, impact our effective tax rate. The complexity of our tax situation is further discussed in Management's Discussion and Analysis in our Annual Report on Form 10-K. Our business plan is

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based on factors of which our Board is aware at the time it is established. If our actual results are affected by discrete events that we did not anticipate, and if we believe these are events for which our management should not bear the responsibility or the benefit in the current period, the impact of such events is eliminated. We use this single metric for the determination of the incentive compensation for all of our executives, although we may adjust individual compensation based on our assessment of individual performance. We believe that the use of a single metric for all executives motivates our executives to work cohesively to achieve our goal and think the benefits of this concerted effort among our executive team outweigh the marginal additional performance that we could possibly motivate on an individual basis with personal performance targets.

In December 2006, the Compensation Committee approved the 2007 cash incentive plan for executive officers (other than the Vice President Marketing and Sales) of the Company based on the Company achieving the pre-tax profit contained in the 2007 business plan adopted by our Board of Directors. The target bonus for the Chief Executive Officer was set at 75% of 2007 base salary and the target bonus for the other executive officers was set at 35% of their respective 2007 base salaries. The Chief Executive Officer's cash bonus could have ranged from 37.5% to a maximum of 112.5% of 2007 base salary, and the cash bonuses for the other executive officers could have ranged from 17.5% to a maximum of 52.5% of their respective 2007 base salaries. The incentive plan bonuses would have been paid at the lowest end of the range for achieving pre-tax profits of 85% of the amount included in the 2007 business plan, would have been paid to the target level of incentive payment if pre-tax profits were equal to the amount contained in the business plan, and would have been paid at the highest end of the range if pre-tax profit equaled or exceeded 115% of the business plan. Incentive plan payments would have been prorated for results falling in between these milestones. For 2007, we did not make any incentive payments. Our pre-tax profits, as adjusted to eliminate, primarily, the loss incurred from operating Excel-Tech for one month and from foreign exchange losses incurred in hedging the purchase price for Excel-Tech that was payable in Canadian dollars, as well as other expenses related to the acquisition, was approximately 84% of the pre-tax profit contained in the business plan and, therefore, no incentive payments were earned under the plan. At an April 2007 meeting the Compensation Committee approved the non-salary cash compensation for our Vice President Marketing and Sales, providing for commissions at specified percentages of sales, based on achieving a pre-determined threshold level of sales, and an incentive based on achievement of Company sales goals and on the attainment of the pre-tax earnings measure that is contained in the business plan approved by our board of directors for the operation of our business for the full year.

In December 2007, the Compensation Committee approved the 2008 cash compensation for the executive officers. Salary increases were 4%, 16%, 11% and 14% for Dr. Chung, Mr. Mince, Mr. Murphy and Mr. Traverso, respectively. These changes were based on our ongoing intent to maintain salaries at the median level of our peer group, as adjusted for the Compensation Committee's assessment of individual performance. The Committee also approved the 2008 incentive plan. The plan for Mr. Hawkins has the same percentage minimums, targets and maximums as described above for the 2007 incentive plan. The target bonus for Dr. Chung, Mr. Mince, and Mr. Murphy was increased to 40% of their 2008 base salary, and can range from a minimum of 20.0% to a maximum of 60.0% of their respective 2008 base salaries. Mr. Traverso's target bonus is 27% of his 2008 base salary, and can range from a minimum of 13.5% to a maximum of 40.5% of his respective 2008 base salary. In addition to his 2008 base salary, Mr. Traverso will receive payments pursuant to a sales commission plan that is paid on a regular basis with a target amount of \$65,000, and a minimum and maximum of \$32,500 and \$97,500, respectively. Payment of any bonus under the 2008 incentive plan is, once again, based on the attainment of the pre-tax profits contained in the Board's 2008 business plan.

We believe that the 2008 business plan was developed by the Board using the same philosophy as was employed in setting the plans for 2006 and 2007. For 2006 our pre-tax profit exceeded the business plan by approximately 11% and incentive payments were made accordingly, and for 2007 pre-tax profits did not meet the threshold of 85% of the business plan's pre-tax profits and no incentive awards were paid under our 2007 incentive plan for executives.

### **Equity-Based Compensation Element**

Equity based compensation provides employees with a common interest with our stockholders to increase the value of our common stock. Equity awards are granted to employees, including our executive officers, in the form of stock options and restricted stock, which in the case of options are granted with an exercise price equal to the fair market value on the date of grant. Stock options have value only if the stock price increases over time and the value of restricted stock awards increases over time as the stock price increases. In addition, equity grants help retain key employees because they typically cannot be fully exercised or are subject to a right of repurchase for four years and, in the case of options, if not exercised, are forfeited if the employee leaves the employ of the Company. The four-year vesting schedule also helps focus our employees on long-term performance. In 2006, our Board of Directors reduced the term of options that we grant from ten years to six years in order to reduce the expense of such options under SFAS 123R.

We intend to grant equity awards to our executives having an SFAS 123R value that is consistent with the median value of equity awards made by our peer group. Since 2006, we have sought to achieve this through stock option grants and restricted stock awards, with each form of the annual award representing approximately half of the targeted value for that year.

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Equity-based compensation is granted to executive officers when the executive first joins us. Additional equity based compensation may be granted in connection with a significant change in responsibilities. Further, we typically make annual equity

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awards to our executive officers, as was the case in 2007 based on the factors noted above. The committee's procedure for timing of equity awards (restricted stock and stock options) provides assurances that grant timing is not being manipulated to result in a price that is favorable to employees. We generally expect to make annual equity awards at the Compensation Committee meeting held in connection with the Company's annual meeting. The exercise price for all option grants is the closing price on the last completed day of trading prior to any meeting of the Compensation Committee.

### **Compensation of the Chief Executive Officer**

Mr. Hawkins' compensation in 2007 consisted of the same components as for our other executive officers, including a base salary, incentive compensation and equity compensation. The same principles were employed in establishing Mr. Hawkins' salary, bonus opportunity and equity awards for 2007 as for the other executive officers, as described above. We arrived at Mr. Hawkins' annual salary for 2007, which was an increase of 10% from his base salary for 2006, based on our goal of paying salaries at the median of our peer group companies. Mr. Hawkins' bonus opportunity was based on achievement of pre-tax operating profit as discussed above. Because we did not meet the threshold performance level for payment under our 2007 incentive plan, Mr. Hawkins did not receive an incentive award for 2007. Mr. Hawkins received a restricted stock award of 30,000 shares and a stock option grant of 60,000 shares on June 13, 2007, which awards were designed to match the median level of CEO compensation in our peer group. For 2008, Mr. Hawkins' salary increased by 13% to maintain his salary at the median level of our peer group.

### **Employment Agreements and Change in Control Arrangements**

We entered into employment agreements with William M. Mince and Kenneth M. Traverso in November 2002, with D. Christopher Chung, M.D. in March 2003, with Steven J. Murphy in May 2003 and with James B. Hawkins in April 2004, which agreement was amended in April 2008. Other than Mr. Hawkins, the terms of these agreements are substantially the same. Upon termination of employment for cause, death or disability, the executive will only be eligible for severance benefits, if any, in accordance with the Company's established policies for all employees as then in effect, which consist primarily of short-term disability and group life insurance benefits.

Should an officer's, other than Mr. Hawkins', employment with us terminate for other than cause, death or disability, the officer shall be entitled to:

Receive continuing payments of severance pay, less applicable withholding taxes, at a rate equal to the officer's then current base salary rate for a period of twelve months;

The immediate vesting of any unvested stock options, restricted stock, or other equity awards, which in the case of stock options would be exercisable for a period of 30 days after such termination; and

Continued payment by the Company of COBRA benefits through the lesser of (i) eighteen months from the effective date of such termination, (ii) the date upon which the officer and the officer's eligible dependents become covered under similar plans, or (iii) the date the officer no longer constitutes a Qualified Beneficiary, as such term is defined in Section 4980B(g) of the Internal Revenue Code of 1986, as amended.

These agreements also provide for the same severance benefits as above if the officer terminates his employment for good reason within 12 months following a change-in-control transaction. Employment termination is for good reason if it follows a significant reduction in the officer's duties or responsibilities, a reduction in base salary, a material reduction in employee benefits, relocation of more than 35 miles from the officer's present location, or the failure of a successor entity to assume the employment agreement. A change in control for such employment agreements is a transaction by which someone acquires more than 50% of the Company's outstanding voting power, a change in the Board of Directors within a two year period such that fewer than a majority are incumbent directors, a merger or consolidation following which the stockholders of the Company own 40% or less of the combined voting power of the Company or the surviving entity, or the sale of all or substantially all of the assets of the Company.

Should Mr. Hawkins' employment with us terminate for other than cause, death or disability, Mr. Hawkins shall be entitled to:

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Receive a lump sum payment due and payable within thirty (30) days after the date of separation, less applicable withholding taxes equal to his then current base salary;

The immediate vesting of any unvested stock options, restricted stock, or other equity awards, which in the case of stock options would be exercisable for a period of 30 days after such termination; and

Continued payment by the Company of COBRA benefits through the lesser of (i) twelve months from the effective date of such termination, or (ii) the date upon which he or his eligible dependents become covered under similar plans.

Pursuant to the amendment to Mr. Hawkins employment agreement in April 2008, the agreement provides that if within twelve months of a change-in-control transaction Mr. Hawkins terminates his employment for good reason or is terminated without cause, then Mr. Hawkins will receive a lump sum payment due and payable within thirty (30) days after the date of separation, less

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applicable withholding taxes, equal to two times the sum of (i) the greater of his then current base salary rate and his base salary rate in effect immediately prior to the change-in-control transaction and (ii) the greater of 100% of his target bonus then in effect and 100% of his target bonus as in effect immediately prior to the change-in-control transaction; (iii) continued provision of COBRA or similar benefits through the lesser of twenty-four months or the date upon which Mr. Hawkins becomes covered under similar plans; and (iv) the immediate vesting of unvested stock options, restricted stock and other equity awards. Employment termination is for good reason if it follows a material reduction in the officer's duties or responsibilities, a material reduction in base salary, a material reduction in employee benefits, relocation of more than 35 miles from the officer's present location, or the failure of a successor entity to assume the employment agreement. A change in control for purposes of this employment agreement is a transaction by which someone acquires more than 50% of the Company's outstanding voting power, a merger or consolidation following which the stockholders of the Company own 40% or less of the combined voting power of the Company or the surviving entity, stockholder approval of a plan to liquidate the Company, or the sale of all or substantially all of the assets of the Company.

To be eligible for termination benefits, the executive must comply with certain non-compete and non-solicitation provisions and retention is conditioned on execution of a release of claims.

The base salaries for our executive officers for 2007 were as follows: James B. Hawkins, \$375,000; Steven J. Murphy, \$225,000; D. Christopher Chung, \$230,000; William M. Mince, \$225,000; and Kenneth M. Traverso, \$210,000.

We believe that these agreements appropriately balance our needs to offer a competitive level of severance protection to our executives and to induce our executives to remain in our employ through the potentially disruptive conditions that may exist around the time of a change in control, while not unduly rewarding executives for a termination of their employment. We note that our change in control terms include so-called double trigger provisions, so that the executive is not entitled to the severance payment by the mere occurrence of the change in control. This feature, we believe, will be an incentive to the executive to remain in the employ of the company if such continuation is required by our partner in a change in control transaction. Our Compensation Committee approved the amendment of Mr. Hawkins agreement in April 2008 to provide for two years of salary and bonus payments, and two years of COBRA, or similar, coverage following a review of the change in control severance provisions of the chief executive officers of peer companies. The Committee determined that the prior provision of one year of salary and COBRA benefits was lower than that provided by most of the peer companies and that two years of salary and bonus and benefits was more consistent with that provided by the peer companies.

Our 1991 Stock Option Plan and our Amended and Restated 2000 Stock Awards Plan provide for the grant of options to purchase our common stock to employees and consultants. Prior to June 14, 2006, options granted to employees had a contractual term of ten years; options granted since June 14, 2006 have a contractual term of 6 years. The plans provide that after certain change in control events (as defined in the plan), including, for example, our merger with or into another corporation or the sale of all or substantially all of our assets, outstanding options may be assumed or equivalent options may be substituted, by the successor corporation. Thereafter, if the optionee's status as our employee or employee of the successor corporation is terminated within 12 months other than by a voluntary resignation or termination for cause, the option may become fully exercisable. Further, if the successor corporation does not assume an outstanding option or substitute for it an equivalent option, the option becomes fully vested and exercisable.

For further detailed financial information concerning the severance and change in control arrangements with our executive officers, please see the tabular information contained in the section entitled Potential Payments Upon Termination or Change in Control.

### **Other Benefits**

Executive officers are eligible to participate in all of our employee benefit plans, such as medical, dental, vision, group life, disability, and accidental death and dismemberment insurance, and our 401(k) plan, in each case on the same basis as other employees, subject to applicable law. We also provide vacation and other paid holidays to all employees, including our executive officers, which we intend to be comparable to those provided at peer companies.

### **Accounting Treatment**

We account for equity compensation paid to our employees under SFAS 123R, which requires us to estimate and record an expense over the service period of the award. Our cash compensation is recorded as an expense at the time the obligation is accrued. We structure the cash compensation element of our incentive compensation so that it is taxable to our executives at the time it becomes available to them. We currently intend that all cash compensation paid will be tax deductible by us. However, with respect to equity compensation awards, while any gain recognized by employees from nonqualified options granted at fair market value should be deductible, to the extent that an option constitutes an incentive stock option, gain recognized by the optionee will not be deductible if there is no disqualifying disposition by the optionee. In addition, if we grant restricted stock or restricted stock unit awards that are not subject to performance vesting, they may not be fully deductible by us at

the time the award is otherwise taxable to employees.



**Table of Contents****Tax Deductibility of Executive Compensation**

Section 162(m) of the Internal Revenue Code of 1986, as amended, provides that compensation in excess of \$1 million paid to the chief executive officer or to any of the other four most highly compensated executive officers of a company will not be deductible for federal income tax purposes unless such compensation is paid pursuant to one of the enumerated exceptions set forth in Section 162(m). Our primary objective in designing and administering compensation policies is to support and encourage the achievement of our long-term strategic goals and to enhance stockholder value. When consistent with this compensation philosophy, we also intend to attempt to structure compensation programs such that compensation paid thereunder will be tax deductible by Natus. In general, stock options granted under our stock option plans are intended to qualify under and comply with the performance based compensation exemption provided under Section 162(m), thus excluding from the Section 162(m) compensation limitation any income recognized by executives pursuant to such stock options. The Compensation Committee intends to review periodically the potential impacts of Section 162(m) in structuring and administering our compensation programs.

**SUMMARY COMPENSATION TABLE**

The following table sets forth information concerning compensation of our Chief Executive Officer, Chief Financial Officer, and the other three most highly compensated executive officers (the named executive officers), all of whom were serving as executive officers of the Company as of December 31, 2007.<sup>1</sup>

Name and Principal Position	Year	Salary (2)	Stock Awards (3)	Option Awards (3)	Non-Equity Incentive Plan	All Other Compensation	Total
					(4)	(5)	
James B. Hawkins President and Chief Executive Officer	2007	\$ 375,000	\$ 102,601	\$ 287,230		\$ 3,466	\$ 768,297
	2006	340,000	21,003	299,750	\$ 230,500	2,720	893,973
Steven J. Murphy Vice President Finance and Chief Financial Officer	2007	\$ 225,000	\$ 35,144	\$ 86,640		\$ 4,306	\$ 351,090
	2006	200,000	7,501	81,451	\$ 81,400	2,576	372,928
D. Christopher Chung, M.D. Vice President Medical Affairs and R&D	2007	\$ 230,000	\$ 35,143	\$ 86,416		\$ 2,920	\$ 354,479
	2006	210,000	7,501	79,958	\$ 85,500	2,605	385,564
William M. Mince Vice President Operations	2007	\$ 225,000	\$ 35,143	\$ 85,574		\$ 4,306	\$ 350,023
	2006	201,000	7,501	79,837	\$ 81,800	2,578	372,716
Kenneth M. Traverso Vice President, Marketing and Sales	2007	\$ 299,000	\$ 35,143	\$ 86,416		\$ 3,130	\$ 423,689
	2006	296,000	7,501	85,477	\$ 40,000	2,720	431,698

- (1) Each of the named executive officers has an Employment Agreement with us that provided for an initial base salary that is subject to subsequent review and to adjustments. These agreements provide that the executive's employment is on an at will basis. These agreements also provide for certain payments and other benefits upon termination of employment in certain circumstances, as further described under Employment Agreements and Change in Control Arrangements in the Compensation Discussion and Analysis above, and in the Potential Payments Upon Termination or Change in Control section below.
- (2) For Mr. Traverso, the amount included in the Salary column consists of a base salary plus a commission that is based on sales of the Company that is paid quarterly during the year.
- (3) The amounts included in the Stock Awards and Option Awards columns represent the compensation cost recognized by the Company in 2007 related to restricted stock awards and option awards, respectively, pursuant to Statement of Financial Accounting Standards No. 123R, except that in the case of option awards, a forfeiture rate of zero percent has been used. For a discussion of other valuation assumptions, see Notes 1 and 11 to our consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2007. See the Grants of Plan Based Awards Table for more information regarding the equity awards granted by the Company in 2007. Refer to the Compensation Discussion and Analysis above for a discussion of these awards.

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- (4) No bonuses were paid under our 2007 cash incentive plan for 2007 performance. For 2006, the amounts shown represent amounts paid in March 2007 under our 2006 cash incentive plan for 2006 performance. See the Grants of Plan Based Awards Table for more information regarding non-equity incentive plan compensation. Refer to the Compensation Discussion and Analysis above for a discussion of non-equity incentive plan compensation.
- (5) The amounts included in the All Other Compensation column consist of matching contributions paid by the Company into our 401(k) plan on behalf of the named executive officers and life insurance premiums.

**Table of Contents****GRANTS OF PLAN BASED AWARDS**

This table discloses the actual numbers of stock options and restricted stock awards granted to our Named Executive Officers in 2007 and the grant date fair value of these awards. It also captures potential future payouts under the Company's 2007 non-equity incentive plan.

Name	Grant Date	Estimated Future Payouts Under Non-equity Incentive Plan Awards (1)			All Other Stock Awards: Number of Shares of Stock or Units (2)	All Other Option Awards: Number of Securities Underlying Options (3)	Exercise or Base Price of Option Awards (\$/Share)	Grant Date Fair Value of Stock and Option Awards (\$) (4)
		Threshold (\$)	Target (\$)	Maximum (\$)				
Mr. Hawkins	06/13/2007	\$ 140,625	\$ 281,250	\$ 421,875	30,000		\$ 477,570	
	06/13/2007							
Mr. Murphy	06/13/2007	39,375	78,750	118,125	10,000		159,190	
	06/13/2007							
Dr. Chung	06/13/2007	40,250	80,500	120,750	10,000		159,190	
	06/13/2007							
Mr. Mince	06/13/2007	39,375	78,750	118,125	10,000		159,190	
	06/13/2007							
Mr. Traverso	06/13/2007				10,000		159,190	
	06/13/2007							

- (1) Each of the named executive officers other than Mr. Traverso had a range of payouts targeted for 2007 non-equity incentive compensation, based on the Company's performance as described in Compensation Discussion and Analysis above. No bonus payment was made for 2007 performance.
- (2) Each of the named executive officers received a grant of restricted shares in 2007. The restricted shares vest as follows: 50% in August 2009, 25% in August 2010, and 25% in August 2011.
- (3) Each of the named executive officers received a grant of stock options in 2007. Options were granted with an exercise price equal to the fair market value on the date of grant, which was based on the closing price of the Company's common stock immediately prior to the award. The shares vest ratably over a 48-month period and may be exercised for six years from the date of grant. Refer to the Compensation Discussion and Analysis above for a description of our equity based compensation practices.
- (4) These amounts represent the grant date fair value, computed in accordance with SFAS no. 123R, of restricted stock, restricted stock units and stock options granted to our named Executive Officers in 2007. The assumptions we use in calculating these amounts are discussed in Note 11 Share Based Compensation of the Notes to our consolidated financial statements, except that the amounts reflected in the table above exclude the impact of estimated forfeitures of equity awards.

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## OUTSTANDING EQUITY AWARDS AT FISCAL YEAR-END

Name	Option Awards (1)					Stock Awards	
	Number of Securities Underlying Unexercised Options (#) Exercisable	Number of Securities Underlying Unexercised Options (#) Unexercisable	Option Exercise Price (\$)	Option Expiration Date		Number of Shares or Units of Stock That Have Not Vested (#)	Market Value of Shares or Units of Stock That Have Not Vested (\$)(5)
Mr. Hawkins	7,500	52,500	\$ 15.92	06/13/2013	(4)	44,000	\$ 851,400
	30,000	50,000	11.32	06/15/2012	(4)		
	75,000	45,000	10.03	06/09/2015	(3)		
	406,666	58,334	4.07	04/08/2014	(2)		
Mr. Murphy	2,500	17,500	\$ 15.92	06/13/2013	(4)	15,000	\$ 290,250
	11,250	18,750	11.32	06/15/2012	(4)		
	31,250	18,750	10.03	06/09/2015	(3)		
	38,333	1,667	4.51	02/25/2014	(3)		
	35,000		4.11	05/30/2013	(3)		
	25,000		3.45	11/12/2012	(2)		
Dr. Chung	2,500	17,500	\$ 15.92	06/13/2013	(4)	15,000	\$ 290,250
	11,250	18,750	11.32	06/15/2012	(4)		
	31,250	18,750	10.03	03/09/2015	(3)		
	47,917	2,083	4.51	02/25/2014	(3)		
	50,000		3.50	02/27/2013	(3)		
	25,000		3.45	11/12/2012	(3)		
	10,000		4.70	04/12/2012	(3)		
	50,000		6.25	12/12/2010	(2)		
Mr. Mince	2,500	17,500	\$ 15.92	06/13/2013	(4)	15,000	\$ 290,250
	11,250	18,750	11.32	06/15/2012	(4)		
	31,250	18,750	10.03	06/09/2015	(3)		
	22,917	2,083	4.51	02/25/2014	(2)		

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Mr. Traverso	2,500	17,500	\$ 15.92	06/13/2013	(4)	15,000	\$ 290,250
	11,250	18,750	11.32	06/15/2012	(4)		
	31,250	18,750	10.03	06/19/2015	(3)		
	47,917	2,083	4.51	02/25/2014	(3)		
	50,000		3.50	02/27/2013	(3)		
	50,000		3.45	11/12/2012	(3)		
	25,000		4.15	06/14/2012	(3)		
	10,000		5.69	10/23/2011	(3)		
	100,000		6.25	12/12/2010	(2)		

- (1) Initial grants of options to the named executive officers upon employment vest 6/48ths after the completion of six months of service with the remainder vesting ratably over the next 42 months. Subsequent grants of options vest ratably over a 48-month period.
- (2) Represents an initial grant of options upon employment that expire 10 years from the date of grant.
- (3) Represents subsequent grant of options granted prior to June 14, 2006 that expire 10 years from the date of grant.
- (4) Represents subsequent grant of options granted on or after June 14, 2006 that expire 6 years from the date of grant.
- (5) The amounts in this column represent the value of these awards based on the closing price of our stock on December 31, 2007 of \$19.35.

**OPTION EXERCISES AND STOCK VESTED**

The following table sets forth certain information regarding options and stock awards exercised and vested, respectively, during 2007 for the named executive officers.

Name	Option Awards		Stock Awards	
	Number of Shares Acquired on Exercise (#)	Value Realized on Exercise (\$)	Number of Shares Acquired on Vesting (#) (1)	Value Realized on Vesting (\$)
Mr. Hawkins				
Mr. Murphy				
Dr. Chung				
Mr. Mince				
Mr. Traverso				

- (1) The named executive officers were granted restricted shares on June 13, 2007 that vest 50% in August 2009, 25% in August 2010, and 25% in August 2011.



**Table of Contents****POTENTIAL PAYMENTS UPON TERMINATION OR CHANGE IN CONTROL**

Under the employment agreements between the Company and the named executive officers, upon termination of employment for cause, death or disability, the executive will only be eligible for severance benefits, if any, in accordance with the Company's established policies for all employees as then in effect. The table that follows reflects the amount of compensation due to our named executive officers if their employment is terminated for other than cause, death or disability, or their employment is terminated or the executive terminates his employment for good cause, following a change in control, as more fully described under "Employment Agreements and Change in Control Arrangements" in the "Compensation Discussion and Analysis" above. The amounts shown below assume that such termination or change in control event was effective as of December 31, 2007 and do not give effect to the changes in salary and target bonus for 2008 as more fully described under "Cash Compensation Element" and "Compensation of the Chief Executive Officer" in the "Compensation Discussion and Analysis" above.

Name	Cash Severance Payment	Continuation of Medical and Welfare Benefits	Acceleration of Equity Awards (1)	Total Termination Benefits
Mr. Hawkins (2)	\$ 375,000	\$ 9,825	\$ 2,743,719	\$ 3,128,544
Mr. Murphy	225,000	9,825	700,326	935,151
Dr. Chung	230,000	15,136	892,000	1,137,136
Mr. Mince	225,000	9,825	706,500	941,325
Mr. Traverso	210,000	15,136	706,500	931,636

- (1) Under the employment agreements between the Company and the named executive officers, upon a covered termination, any unvested stock options, restricted stock, or other equity awards would immediately vest and options would be exercisable for up to 30 days following termination. Such unvested awards would also vest if an acquiring company does not assume them following a change in control transaction. The amounts in this column represent the intrinsic value of these awards based on the closing price of our stock on December 31, 2007 of \$19.35.
- (2) Does not give effect to the amendment of Mr. Hawkins employment agreement adopted in April 2008 as more fully described under "Employment Agreements and Change in Control Arrangements" in the "Compensation Discussion and Analysis" above. Under the terms of Mr. Hawkins revised employment agreement, his cash severance payment would be \$1,031,250, the continuation of medical and welfare benefits would be \$19,650 and his total termination benefits would be \$3,794,619.

**DIRECTOR COMPENSATION**

Directors who are employees receive no additional compensation for serving on the board or its committees. The table below discloses the annual compensation provided during the year ended December 31, 2007 to directors who are not employees:

Name	Fees Earned or Paid in			Total (\$)
	Cash (\$ (1))	Stock Awards (\$ (2))	Option Awards (\$ (3, 4))	
Ms. Engibous	\$ 27,500	\$ 25,033	\$ 34,426	\$ 86,959
Mr. Gunst	50,000	25,033	35,650	110,683
Mr. Ludlum	42,250	25,033	33,313	100,596
Mr. Michael	36,250	25,033	34,426	95,709
Mr. Moore	31,250	25,033	33,313	89,596

- (1) Fees earned and paid in cash were based on the following retainer and payment schedule:

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	Prior to Oct. 2007	After Oct. 2007
Annual retainer	\$ 12,000	\$ 20,000
Annual retainer for service as Chairman of the Board	12,000	20,000
Annual retainer for service as Chairman of the Audit Committee	12,000	13,000
Annual retainer for service as Chairman of the Compensation Committee	4,000	6,000
Annual retainer for service as Chairman of the Nominating & Governance Committee	3,000	4,000
Payment for each Board meeting attended	1,500	1,500
Payment for each Audit Committee meeting attended	1,000	1,500
Payment for each Committee meeting attended (excluding the Audit Committee)	500	1,000

In addition, we pay the Audit Committee Chairman \$500 per meeting attended for attendance at Sarbanes-Oxley Oversight meetings.



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- (2) In June 2007, each non-employee director received a restricted stock award of 2,500 shares that vests in June 2008. The grant date fair value of these awards, computed in accordance with SFAS 123R, was \$39,800. The assumptions we use in calculating this amount are discussed in Note 11 of the notes to our consolidated financial statements included in our Annual Report on Form 10-K, except that this amount excludes the impact of estimated forfeitures of equity awards. In 2006, each non-employee director received a restricted stock award of 1,250 shares that vested in June 2007. The amount in this column shows the expense recognized by the Company in 2007 for restricted stock awards.
- (3) The amounts in this column reflect the expenses related to options granted to the Company's non-employee directors recognized in the Company's 2007 financial statements pursuant to Statement of Financial Accounting Standards No. 123R, except that a forfeiture rate of zero percent has been used. For a discussion of other valuation assumptions, see Notes 1 and 11 to our consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2007. All of our non-employee Directors received an initial grant of 30,000 options upon their appointment to the board that vests ratably over a 36-month period. Any non-employee directors appointed to the board in the future will receive an initial grant of 10,000 shares that vests ratably over a 36-month period. Prior to December 31, 2006, each director received an additional grant of 10,000 options annually. For 2006, each director received a grant of 7,500 options and restricted stock as discussed above and for 2007, each director received a grant of 5,000 options and restricted stock as discussed above. All options granted to directors other than their initial grant vest ratably over a 12-month period. Stock option grants were established using the same procedure for timing and price as is used for employees. Refer to the Compensation Discussion and Analysis above for a description of our equity based compensation practices. The grant date fair value of the options granted to our non-employee directors in 2007, computed in accordance with SFAS 123R, was \$31,446. The assumptions we use in calculating this amount are discussed in Note 11 of the notes to our consolidated financial statements included in our Annual Report on Form 10-K, except that this amount excludes the impact of estimated forfeitures of equity awards.
- (4) At December 31, 2007, Ms. Engibous had 52,500 options and 2,500 unvested restricted shares outstanding, Mr. Gunst had 47,500 options and 2,500 unvested restricted shares outstanding, Mr. Ludlum had 5,000 options and 2,500 unvested restricted shares outstanding, Mr. Michael had 52,500 options and 2,500 unvested restricted shares outstanding, and Mr. Moore had 72,500 options and 2,500 unvested restricted shares outstanding.

**Compensation Committee Interlocks and Insider Participation**

Our Compensation Committee consists of Mr. Moore, Ms. Engibous and Mr. Gunst. Mr. Moore was our Chief Executive Officer from April 1989 to May 1992. During 2007, Mr. Hawkins, our president and chief executive officer, participated in discussions and decisions of the Compensation Committee regarding salaries and incentive compensation for our executive officers, but he was excluded from discussions regarding his own salary and incentive compensation. No interlocking relationship exists between any member of our Compensation Committee and any member of any other company's board of directors or compensation committee.

**REPORT OF THE COMPENSATION COMMITTEE OF THE BOARD OF DIRECTORS**

**Compensation Committee Report**

The Compensation Committee of the Board of Directors of Natus has reviewed and discussed the Compensation Discussion and Analysis required by Item 402(b) of Regulation S-K with management and, based on such review and discussions, the Compensation Committee recommended to the Board that the Compensation Discussion and Analysis be included in the Company's definitive Proxy Statement relating to its 2008 Annual Meeting of Stockholders.

Respectfully submitted by:  
THE COMPENSATION COMMITTEE

WILLIAM M. MOORE, Chairman  
DORIS E. ENGIBOUS  
ROBERT A. GUNST



**Table of Contents****ITEM 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters. Equity Compensation Plan Information**

The following table provides information as of December 31, 2007 about our common stock that may be issued upon the exercise of options, warrants, and rights under all of our existing equity compensation plans, including the 1991 Stock Option Plan, 2000 Stock Awards Plan, 2000 Supplemental Stock Option Plan, 2000 Director Option Plan, and 2000 Employee Stock Purchase Plan, each as amended.

Plan Category	Number of Securities to be Issued upon Exercise of Outstanding Options, Warrants and Rights	Weighted-Average Exercise Price of Outstanding Options, Warrants and Rights	Number of Securities Remaining Available for Future Issuance under Equity Compensation Plans (excluding securities reflected in the first column)
Equity compensation plans approved by security holders	2,879,667	\$ 8.23	9,984,319
Equity compensation plans not approved by security holders			
<b>Total</b>	<b>2,879,667</b>	<b>\$ 8.23</b>	<b>9,984,319</b>

Of the shares of common stock to be issued upon exercise of outstanding options, warrants, and rights, 18,009 shares related to outstanding options under our 1991 Stock Option Plan, 2,494,658 shares related to outstanding options under our 2000 Stock Awards Plan, 150,000 shares related to outstanding options under our 2000 Supplemental Stock Option Plan, and 230,000 shares related to outstanding options under our 2000 Director Option Plan.

Of the shares of common stock remaining available for future issuance under equity compensation plans, 4,996,564 shares remained available for future issuance under our 2000 Stock Awards Plan, 586,142 shares remained available for future issuance under our 2000 Director Option Plan, and 4,401,613 shares remained available for future issuance under our 2000 Employee Stock Purchase Plan. The 1991 Stock Option Plan and 2000 Supplemental Stock Option Plan were terminated as to new grants in July 2001. The number of shares reserved for issuance pursuant to our 2000 Stock Awards Plan is subject to an automatic increase on the first day of our fiscal year in an amount equal to the lesser of (a) 1,500,000 shares of common stock; (b) 7% of our outstanding shares of common stock on the last day of the prior fiscal year; or (c) an amount determined by our board of directors. The number of shares reserved for issuance pursuant to our 2000 Director Option Plan is subject to an automatic increase on the first day of our fiscal year in an amount equal to the lesser of (a) 100,000 shares of common stock; (b) one-half of one percent of our outstanding shares of common stock on the last day of the prior fiscal year; or (c) an amount determined by our board of directors. The number of shares reserved for issuance pursuant to our 2000 Employee Stock Purchase Plan is subject to an automatic increase on the first day of our fiscal year in an amount equal to the lesser of (a) 650,000 shares of common stock; (b) 4% of our outstanding shares of common stock on the last day of the prior fiscal year; or (c) an amount determined by our board of directors. We are unable to ascertain with specificity the number of securities to be issued upon exercise of outstanding rights under, or the weighted average exercise price of outstanding rights under, the 2000 Employee Stock Purchase Plan.

**SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT**

The following table sets forth information, as of April 25, 2008, concerning:

Beneficial owners of more than 5% of Natus common stock;

Beneficial ownership by current Natus directors and nominees, and the named executive officers set forth in the Summary Compensation Table ; and

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Beneficial ownership by all current Natus directors and executive officers as a group.

The information provided in the table is based on Natus records, information filed with the Securities and Exchange Commission and information provided to Natus, except where otherwise noted.

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The number of shares beneficially owned by each entity, person, director or executive officer is determined under rules of the Securities and Exchange Commission, and the information is not necessarily indicative of beneficial ownership for any other purpose. Under such rules, beneficial ownership includes any shares as to which the individual has the sole or shared voting power or investment power and also any shares that the individual has the right to acquire as of June 24, 2008 (60 days after April 25, 2008) through the exercise of any stock option or other right. The address for those individuals for which an address is not otherwise provided is c/o Natus Medical Incorporated, 1501 Industrial Road, San Carlos, California 94070. Unless otherwise indicated, each person has sole voting and investment power (or shares such powers with his or her spouse) with respect to the shares set forth in the following table.

**SECURITY OWNERSHIP TABLE**

Name and Address	Shares Owned	Right to acquire beneficial ownership under options exercisable within 60 days	Total Owned	
<b>Principal Stockholders</b>				
Nierenberg Investment Management Company, Inc.				
19605 NE 8 <sup>th</sup> Street				
Camas, WA 98607 (1)	4,359,845		4,359,845	19.04%
The Bank of New York Mellon Corporation				
One Wall Street, 31 <sup>st</sup> Floor				
New York, NY 10286 (2)	1,186,302		1,186,302	5.18%
AWM Investment Company, Inc.				
527 Madison Avenue, Suite 2600				
New York, NY 10022 (3)	1,094,861		1,094,861	4.78%
<b>Directors, Nominees and Named Executive Officers</b>				
D. Christopher Chung, M.D. (4)	15,000	242,501	257,501	1.11%
Doris E. Engibous (5)	3,750	52,500	56,250	*
Robert A. Gunst (5)	5,750	47,500	53,250	*
James B. Hawkins (6)	73,667	609,999	683,666	2.91%
Kenneth E. Ludlum (5)	47,450	5,000	52,450	*
Mark D. Michael (5)	8,750	52,500	61,250	*
William L. Mince (7)	69,981	82,501	152,482	*
William M. Moore (8)	111,452	72,500	183,952	*
Steven J. Murphy (7)	32,817	157,501	190,318	*
Kenneth M. Traverso (9)	139,123	342,501	481,624	2.07%
All Directors and Executive Officers as a group (10 persons) (10)	507,740	1,665,003	2,172,743	8.85%

\* Represents holdings of less than one percent.

(1) Based on information reported on Schedule 13D filed with the Securities and Exchange Commission on April 8, 2008. Nierenberg Investment Management Company, Inc. is the general partner of several entities that hold our common stock, including the D<sup>3</sup> Family Bulldog Fund L.P., the D<sup>3</sup> Offshore Fund L.P., the D<sup>3</sup> Family Fund L.P., and the D<sup>3</sup> Family Canadian Fund L.P., collectively, the D<sup>3</sup>

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Family Funds. Nierenberg Investment Management Company has sole voting and investment power with respect to all of these shares.

- (2) Based on information reported on Schedule 13G filed with the Securities and Exchange Commission on February 14, 2008. All of the shares are beneficially owned by The Bank of New York Mellon Corporation and its direct or indirect subsidiaries in their various fiduciary capacities. The Bank of New York Mellon Corporation reports sole voting power with respect to 907,425 shares, shared voting power with respect to 3,000 shares, and sole dispositive power with respect to 1,186,302 shares.
  
- (3) Based on information reported on Schedule 13G filed with the Securities and Exchange Commission on February 13, 2008. AWM Investment Company, Inc. ( AWM ) is the general partner and investment advisor to Special Situations Cayman Fund, L.P. AWM also serves as the general partner of MGP Advisers Limited Partnership, the general partner and investment adviser to Special Situations Fund III, L.P. and general partner of Special Situations Fund III, QP, L.P. ( SSFQP ). AWM serves as the

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investment adviser to SSFQP. AWM reports sole voting and dispositive power with respect to all of these shares. Does not give effect to any transactions in our common stock subsequent to the latest filing on Schedule 13G, including the shares purchased in our underwritten stock offering on April 9, 2008 described in Certain Relationships and Policies on Related Party Transactions above.

- (4) All shares subject to a right of repurchase by the Company that expires as to 2,500 shares on August 1, 2008, 6,250 shares on August 1, 2009, 3,750 shares on August 1, 2010 and 2,500 shares on August 1, 2011.
- (5) Includes 2,500 shares subject to a right of repurchase by the Company that expires on June 13, 2008.
- (6) Includes 44,000 shares subject to a right of repurchase by the Company that expires with respect to 7,000 shares on August 1, 2008, 18,500 shares on August 1, 2009, 11,000 shares on August 1, 2010 and 7,500 shares on August 1, 2011.
- (7) Includes 15,000 shares subject to a right of repurchase by the Company that expires as to 2,500 shares on August 1, 2008, 6,250 shares on August 1, 2009, 3,750 shares on August 1, 2010 and 2,500 shares on August 1, 2011.
- (8) Includes 99,892 shares held by The Moore Family Trust and 4,150 shares held by Mr. Moore's spouse. 101,142 of the shares beneficially owned by Mr. Moore have been pledged as collateral for a line of credit available to Mr. Moore, under which there is currently no outstanding balance. Also includes 2,500 shares subject to a right of repurchase by the Company that expires on June 13, 2008.
- (9) Includes 8,572 shares held by the Traverso Family Trust, 10,500 shares held in an IRA for the benefit of Mr. Traverso and 4,100 shares held in an IRA for the benefit of Mr. Traverso's spouse. 99,951 of the shares beneficially owned by Mr. Traverso have been pledged as collateral for a line of credit available to Mr. Traverso. Also includes 15,000 shares subject to a right of repurchase by the Company that expires as to 2,500 shares on August 1, 2008, 6,250 shares on August 1, 2009, 3,750 shares on August 1, 2010 and 2,500 shares on August 1, 2011.
- (10) Includes all shares referenced in notes 4 through 9 above.

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**SIGNATURES**

Pursuant to the requirements of the Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this Amendment No. 1 to Annual Report on Form 10-K/A, to be signed on its behalf by the undersigned, thereunto duly authorized.

**Natus Medical Incorporated**

By:                               /s/ James B. Hawkins  
                                          James B. Hawkins  
                                          President and Chief Executive Officer

Date: May 21, 2008



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**EXHIBIT INDEX**

<b>Exhibit Number</b>	<b>Description of Document</b>
31.1	Certification of Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

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