DIGIRAD CORP
Form 10-Q
July 27, 2011
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-Q

(Mark One)

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2011

¨ **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: 000-50789

Digirad Corporation

(Exact name of registrant as specified in its charter)

Delaware	**33-0145723**
(State or Other Jurisdiction of Incorporation or Organization)	**(I.R.S. Employer Identification No.)**
13950 Stowe Drive, Poway, CA	**92064**
(Address of Principal Executive Offices)	**(Zip Code)**

(858) 726-1600

(Registrant s Telephone Number, Including Area Code)

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

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

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

Large accelerated filer ¨	Accelerated filer ¨
Non-accelerated filer x (Do not check if a smaller reporting company)	Smaller reporting company ¨

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

As of July 19, 2011, the registrant had 19,340,199 shares of Common Stock ($0.0001 par value) outstanding.

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DIGIRAD CORPORATION

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Digirad Corporation

Consolidated Balance Sheets

(In thousands, except share amounts)

	June 30, 2011 (Unaudited)	December 31, 2010
Assets		
Current assets:		
Cash and cash equivalents	$ 9,369	$ 20,459
Securities available-for-sale	21,771	9,788
Accounts receivable, net	8,077	7,527
Inventories, net	6,061	5,432
Other current assets	832	1,038
Total current assets	46,110	44,244
Property and equipment, net	5,860	7,185
Intangible assets, net	632	808
Goodwill	184	184
Total assets	$ 52,786	$ 52,421
Liabilities and stockholders equity		
Accounts payable	$ 2,332	$ 1,871
Accrued compensation	1,972	1,600
Accrued warranty	403	378
Deferred revenue	2,069	2,379
Other accrued liabilities	2,301	2,096
Total current liabilities	9,077	8,324
Deferred rent	134	138
Total liabilities	9,211	8,462
Commitments and contingencies (Note 9)		
Stockholders equity:		
Preferred stock, $0.0001 par value: 10,000,000 shares authorized; no shares issued or outstanding		
Common stock, $0.0001 par value: 80,000,000 shares authorized; 18,726,561 and 18,597,311 shares issued and outstanding (net of treasury shares) at June 30, 2011 and December 31, 2010, respectively	2	2
Treasury stock, at cost; 573,218 shares at June 30, 2011 and December 31, 2010	(1,039)	(1,039)
Additional paid-in capital	155,216	154,785
Accumulated other comprehensive income (loss)	(137)	63
Accumulated deficit	(110,467)	(109,852)
Total stockholders equity	43,575	43,959
Total liabilities and stockholders equity	$ 52,786	$ 52,421

See accompanying notes to consolidated financial statements.

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Digirad Corporation

Consolidated Statements of Operations

(Unaudited and in thousands, except per share data)

	Three Months Ended June 30,		Six months Ended June 30,	
	2011	2010	2011	2010
Revenues:				
DIS	$ 9,950	$ 9,787	$ 19,546	$ 20,509
Product	4,299	3,372	8,878	7,718
Total revenues	14,249	13,159	28,424	28,227
Cost of revenues:				
DIS	7,772	8,172	15,534	16,974
Product	2,483	3,079	5,376	5,974
Total cost of revenues	10,255	11,251	20,910	22,948
Gross profit	3,994	1,908	7,514	5,279
Operating expenses:				
Research and development	714	870	1,422	1,595
Marketing and sales	1,617	1,551	3,041	3,181
General and administrative	1,866	2,139	3,970	4,400
Amortization of intangible assets	83	107	176	239
Restructuring loss (gain)		352	(164)	352
Total operating expenses	4,280	5,019	8,445	9,767
Loss from operations	(286)	(3,111)	(931)	(4,488)
Other income:				
Interest income	72	88	280	209
Interest expense	(7)	(2)	(20)	(3)
Other income (expense)	(7)	(59)	57	(37)
Total other income	58	27	317	169
Net loss	$ (228)	$ (3,084)	$ (614)	$ (4,319)
Net loss per common share basic and diluted	$ (0.01)	$ (0.16)	$ (0.03)	$ (0.23)
Weighted average shares outstanding basic and diluted	18,988	18,738	18,963	18,704

See accompanying notes to consolidated financial statements.

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Digirad Corporation

Consolidated Statements of Cash Flows

(Unaudited and in thousands)

	Six months Ended June 30, 2011	2010
Operating activities		
Net loss	$ (614)	$ (4,319)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation	1,678	1,920
Amortization of intangible assets	176	239
Provision for bad debt	82	74
Stock-based compensation	423	349
Restructuring loss		164
(Gain) loss on disposal of assets	(41)	78
(Accretion of discount) amortization of premium on securities available-for-sale	(71)	194
Changes in operating assets and liabilities:		
Accounts receivable	(633)	(114)
Inventories	(615)	385
Other assets	206	120
Accounts payable	461	(66)
Accrued compensation	372	227
Other accrued liabilities	(54)	126
Net cash provided by (used in) operating activities	1,370	(623)
Investing activities		
Purchases of property and equipment	(396)	(978)
Proceeds from sale of property and equipment	70	40
Purchases of securities available-for-sale	(13,113)	(2,552)
Maturities of securities available-for-sale	1,000	5,408
Net cash (used in) provided by investing activities	(12,439)	1,918
Financing activities		
Issuances of common stock	9	39
Repurchases of common stock		(49)
Repayment of obligations under capital leases	(30)	(30)
Net cash used in financing activities	(21)	(40)
Net (decrease) increase in cash and cash equivalents	(11,090)	1,255
Cash and cash equivalents at beginning of period	20,459	13,560
Cash and cash equivalents at end of period	$ 9,369	$ 14,815

See accompanying notes to consolidated financial statements.

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DIGIRAD CORPORATION

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Note 1. The Company

Digirad Corporation (Digirad), a Delaware corporation, is a leading developer and manufacturer of medical diagnostic imaging systems including solid-state gamma cameras for nuclear cardiology and general nuclear medicine applications. Digirad is also one of the largest national providers of in-office nuclear cardiology imaging and ultrasound services to physician practices, hospitals and imaging centers through its Digirad Imaging Solutions (DIS) division. Digirad has two reportable segments, DIS and Product which are collectively referred to herein as the Company . The accompanying consolidated financial statements include the operations of both segments. Intercompany accounts and transactions are accounted for at cost and have been eliminated in consolidation. Substantially all of the Company s revenue arises from sales activity in the United States. Through DIS, the Company provides in-office leasing services to physicians, offering certified personnel, required licensure, an imaging system and other support and supplies for the performance of nuclear and ultrasound imaging procedures under the supervision of its physician customers. DIS physician customers enter into annual lease contracts for imaging services generally delivered on a per-day basis. The Company s Product segment sells solid-state gamma cameras and provides camera service and maintenance.

Note 2. Basis of Presentation and Significant Accounting Policies

Basis of Presentation

The Company has prepared the accompanying unaudited consolidated financial statements in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and disclosures required by generally accepted accounting principles for complete financial statements. In the opinion of the Company s management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the six months ended June 30, 2011 are not necessarily indicative of the results that may be expected for the entire year. These consolidated financial statements were derived from and should be read in conjunction with the consolidated financial statements and notes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2010 filed with the Securities and Exchange Commission on March 9, 2011 from which the December 31, 2010 balance sheet information was derived.

Revenue Recognition

The Company derives revenue primarily from providing in-office services to support the performance of cardiac imaging procedures and from selling and servicing solid-state digital gamma cameras. The Company recognizes revenue in accordance with the authoritative guidance for revenue recognition, when all of the following four criteria are met: (i) a contract or sales arrangement exists; (ii) products have been shipped and title has transferred or services have been rendered; (iii) the price of the products or services is fixed or determinable; and (iv) collectability is reasonably assured. The timing of revenue recognition is based upon factors such as passage of title and risk of loss, the need for installation, and customer acceptance. These factors are based on the specific terms of each contract or sales arrangement.

DIS revenue is derived from the leasing of personnel and equipment for in-office nuclear and ultrasound imaging procedures. Revenue related to imaging services is recognized at the time services are performed and collection is reasonably assured. DIS services are generally billed on a per-day basis under annual contracts, which specify the number of days of service to be provided, or on a flat rate month-to-month basis.

Product revenues are generated from the sales of gamma cameras and follow-on maintenance service contracts. The Company generally recognizes revenue upon delivery to customers. The Company also provides installation and training for camera sales in the United States. Installation and training is generally performed shortly after delivery and represents a cost, which the Company accrues at the time revenue is recognized. Neither service is essential to the functionality of the product. Maintenance services are sold beyond the term of the warranty, which is generally one year from the date of purchase. Revenue from these contracts is deferred, recognized ratably over the service period and is included in Product sales.

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Fair-value of Financial Instruments

The authoritative guidance for fair value measurements defines fair value for accounting purposes, establishes a framework for measuring fair value and provides disclosure requirements regarding fair value measurements. The guidance defines fair value as an exit price, which is the price that would be received upon sale of an asset or paid upon transfer of a liability in an orderly transaction between market participants at the measurement date. The degree of judgment utilized in measuring the fair value of assets and liabilities generally correlates to the level of pricing observability. Assets and liabilities with readily available, actively quoted prices or for which fair value can be measured from actively quoted prices in active markets generally have more pricing observability and require less judgment in measuring fair value. Conversely, assets and liabilities that are rarely traded or not quoted have less pricing observability and are generally measured at fair value using valuation models that require more judgment. These valuation techniques involve some level of management estimation and judgment, the degree of which is dependent on the price transparency of the asset, liability or market and the nature of the asset or liability. The Company has categorized its assets and liabilities measured at fair value into a three-level hierarchy in accordance with this guidance. See note 5 for a further discussion regarding the Company s measurement of assets and liabilities at fair value.

Share-Based Compensation

The Company accounts for share-based awards exchanged for services in accordance with the authoritative guidance for share-based payments. Under this guidance, share-based compensation expense is measured at the grant date, based on the estimated fair value of the award, and is recognized as expense, net of estimated forfeitures, over the requisite service period.

Total share-based compensation expense related to all of the Company s share-based awards for the three and six months ended June 30, 2011 and 2010 was allocated in the consolidated statements of operations as follows (in thousands, except per share data):

	Three Months Ended June 30,		Six months Ended June 30,	
	2011	2010	2011	2010
Cost of revenues:				
DIS	$ 4	$ 10	$ 8	$ 18
Product	24	16	53	27
Research and development	20	17	43	26
Marketing and sales	29	31	65	50
General and administrative	119	95	254	228
Share-based compensation expense	$ 196	$ 169	$ 423	$ 349
Share-based compensation expense per share:				
Basic and diluted	$ 0.01	$ 0.01	$ 0.02	$ 0.02

Comprehensive Loss

Comprehensive loss consists of the following components (in thousands):

	Three Months Ended June 30,		Six months Ended June 30,	
	2011	2010	2011	2010
Net loss, as reported	$ (228)	$ (3,084)	$ (614)	$ (4,319)
Unrealized loss on marketable securities	(30)	(276)	(200)	(91)
Comprehensive loss	$ (258)	$ (3,360)	$ (814)	$ (4,410)

New Accounting Pronouncements

In May, 2011, The FASB issued ASU 2011-4, *Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRS*. The objective of this amendment is to achieve common fair value measurement and disclosure requirements in U.S GAAP and IFRS. This amendment is to ensure that fair value has the same meaning in U.S. GAAP and IFRS and that their respective fair value measurement and disclosure requirements are the same. This guidance is effective for the first quarter of 2012. The Company does not expect that this authoritative guidance will have any material effect on the Company s financial statements.

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In June, 2011, The FASB issued ASU 2011-5, *Presentation of Comprehensive Income*. The objective of this amendment is to improve the comparability, consistence, and transparency of financial reporting and to increase the prominence of items reported in other comprehensive income. This guidance is effective beginning with the first quarter of 2012. The Company does not expect that this authoritative guidance will have any material effect on the Company s financial statements.

Note 3. Basic and Diluted Net Income (Loss) Per Share

Basic earnings per share (EPS) is calculated by dividing net income or loss by the weighted average number of common shares and vested restricted stock units outstanding. Diluted EPS is computed by dividing net income or loss by the weighted average number of common shares and vested restricted stock units outstanding and the weighted average number of dilutive common stock equivalents, including stock options and non-vested restricted stock units under the treasury stock method. Common stock equivalents are only included in the diluted earnings per share calculation when their effect is dilutive. Shares used to compute basic net loss per share include 286,706 and 295,975 weighted average vested restricted stock units for the three and six months ended June 30, 2011, respectively, compared to 235,054 and 217,041 for the three and six months ended June 30, 2010, respectively.

Since the Company incurred net losses for the three and six months ended June 30, 2011 and 2010, 674,493 and 637,488 common share equivalents were excluded from the computation of diluted loss per share for the three and six months ended June 30, 2011, respectively, compared to 293,085 and 272,679 for the three and six months ended June 30, 2010, respectively, as their effect would be antidilutive.

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Note 4. Supplementary Balance Sheet Information (in thousands):

	June 30, 2011	December 31, 2010
Inventories, net:		
Raw materials	$ 3,339	$ 3,050
Work-in-process	2,905	2,641
Finished goods	1,697	1,632
	7,941	7,323
Less reserve for excess and obsolete inventories	(1,880)	(1,891)
	$ 6,061	$ 5,432
Property and equipment, net:		
Machinery and equipment	$ 21,454	$ 21,627
Computer hardware and software	2,627	2,417
Leasehold improvements	812	807
	24,893	24,851
Accumulated depreciation	(19,033)	(17,666)
	$ 5,860	$ 7,185
Intangible assets, net:		
Customer relationships	$ 2,600	$ 2,600
Covenants not to compete	300	300
Patents	141	141
	3,041	3,041
Accumulated amortization of customer relationships	(2,082)	(1,942)
Accumulated amortization of covenants not to compete	(250)	(220)
Accumulated amortization of patents	(77)	(71)
	$ 632	$ 808
Other accrued liabilities:		
Radiopharmaceuticals and consumable medical supplies	$ 486	$ 365
Sales and property taxes payable	441	464
Outside services and consulting	365	318
Professional fees	245	284
Facilities and related costs	158	210
Customer deposits	156	144
Travel expenses	98	101
Other accrued liabilities	352	210
	$ 2,301	$ 2,096

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Note 5. Fair Value of Financial Instruments

The Company has categorized its assets and liabilities measured at fair value into a three-level hierarchy in accordance with the authoritative guidance for fair value measurements. Assets and liabilities measured at fair value using quoted prices in active markets for identical assets or liabilities are generally categorized as Level 1; assets and liabilities measured at fair value using observable market-based inputs or unobservable inputs that are corroborated by market data for similar assets or liabilities are generally categorized as Level 2; and assets and liabilities measured at fair value using unobservable inputs that cannot be corroborated by market data are generally categorized as Level 3. Assets and liabilities presented at fair value in the Company s consolidated balance sheets are generally categorized as follows:

Level 1: Quoted prices in active markets for identical assets or liabilities. The Company has U.S. treasury securities which are valued based on publicly available quoted prices for identical securities as of June 30, 2011. The Company did not have any Level 1 assets or liabilities as of December 31, 2010.

Level 2: Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. The Company s Level 2 assets as of June 30, 2011 and December 31, 2010 included its investments in corporate debt securities which were valued by a third party pricing vendor using proprietary valuation models (typically discounted cash flow models) and analytical tools. The inputs to these models related to similar instruments and were both objective and publicly available.

Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Such assets and liabilities may have values determined using pricing models, discounted cash flow methodologies, or similar techniques, and include instruments for which the determination of fair value requires significant management judgment or estimation. The Company did not have any Level 3 assets or liabilities as of June 30, 2011 and December 31, 2010.

As required by the guidance for fair value measurements, financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. Management s assessment of the significance of a particular input to the fair value measurement requires judgment, which may affect the valuation of assets and liabilities and their placement within the fair value hierarchy levels. The following table sets forth by level within the fair value hierarchy the Company s assets and liabilities that were recorded at fair value as of June 30, 2011 and December 31, 2010 (in thousands).

	At Fair Value as of June 30, 2011			
	Level 1	Level 2	Level 3	Total
Assets:				
U.S. treasury securities	$ 13,080	$	$	$ 13,080
Corporate debt securities		8,691		8,691
Total	$ 13,080	$ 8,691	$	$ 21,771

	At Fair Value as of December 31, 2010			
	Level 1	Level 2	Level 3	Total
Assets:				
Corporate debt securities	$	$ 9,788	$	$ 9,788

Cash Equivalents

The Company considers all investments with a maturity of three months or less when acquired to be cash equivalents. Cash equivalents primarily are funds invested in money market funds and U.S. treasury securities whose cost equals fair market value.

Securities Available for Sale

Securities available-for-sale consists of investment grade corporate debt and U.S. treasury securities. The Company classifies all securities as available-for-sale, as the sale of such securities may be required prior to maturity to implement management strategies. These securities are carried at fair value, with the unrealized gains and losses reported as a component of other comprehensive income (loss) in stockholder s equity until realized. Realized gains and losses from the sale of available-for-sale securities, if any, are determined on a specific identification basis. A decline in the market value of any available-for-sale security below cost that is determined to be other than temporary will result in an impairment charge to earnings and a new cost basis for the security is established. No such impairment charges were recorded for any period presented. Premiums and discounts are amortized or accreted over the life of the

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related security as an adjustment to yield using the straight-line method. Interest income is recognized when earned. Realized gains and losses on investments in securities are included in interest income within the consolidated statements of operations. Realized gains were $0.1 million and $0.3 million during the three and six months ended June 30, 2011, respectively, compared to realized gains of $0.1 million and $0.2 million during the three and six months ended June 30, 2010, respectively. The amortization, accretion and interest income are included in interest income within the accompanying consolidated statements of operations.

The following table sets forth the composition of securities available for sale as of June 30, 2011 and December 31, 2010 (in thousands):

As of June 30, 2011	Maturity in Years	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
U.S. treasury securities	1 or less	$ 13,086	$	$ (6)	$ 13,080
Corporate debt securities	3 or less	8,822	8	(139)	8,691
Total:		$ 21,908	$ 8	$ (145)	$ 21,771

As of December 31, 2010	Maturity in Years	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Corporate debt securities	3 or less	$ 9,851	$ 28	$ (91)	$ 9,788

The Company does not intend to sell the investments in unrealized loss positions as of June 30, 2011. It s not more likely than not that the Company will be required to sell its investments before recovery of their amortized costs. As of June 30, 2011, none of the Company s investments have been in an unrealized loss position for more than 12 months.

Note 6. Warranty

The Company generally provides a 12 month warranty on its gamma cameras. The Company accrues the estimated cost of this warranty at the time revenue is recorded and charges warranty expense to Product cost of revenues. Warranty reserves are established based on historical experience with failure rates and repair costs and the number of systems covered by warranty. Warranty reserves are depleted as gamma cameras are repaired. The costs consist principally of materials, personnel, overhead and transportation. The Company reviews warranty reserves quarterly and, if necessary, makes adjustments.

The Company s activities within the warranty reserve consisted of the following (in thousands):

	Three Months Ended June 30,		Six months Ended June 30,	
	2011	2010	2011	2010
Balance at beginning of period	$ 372	$ 329	$ 378	$ 332
Charges to cost of revenues	242	127	458	309
Costs applied to liability	(211)	(179)	(433)	(364)
Balance at end of period	$ 403	$ 277	$ 403	$ 277

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Note 7. Segments

The Company s reporting segments have been determined based on the nature of the products and services offered to customers or the nature of their function in the organization. The Company evaluates performance based on the operating income contributed by each segment. The accounting policies of the reporting segments are the same as those described in the summary of significant accounting policies in the Company s Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 9, 2011. Segment results are as follows (in thousands):

	Three Months Ended June 30,		Six months Ended June 30,	
	2011	2010	2011	2010
Gross profit by segment:				
DIS	$ 2,178	$ 1,615	$ 4,012	$ 3,535
Product	1,816	293	3,502	1,744
Consolidated gross profit	$ 3,994	$ 1,908	$ 7,514	$ 5,279
Loss from operations by segment:				
DIS	$ (16)	$ (1,282)	$ (308)	$ (2,236)
Product	(270)	(1,829)	(623)	(2,252)
Consolidated loss from operations	$ (286)	$ (3,111)	$ (931)	$ (4,488)
Depreciation and amortization of tangible and intangible assets by segment:				
DIS	$ 821	$ 880	$ 1,692	$ 1,919
Product	77	98	162	240
Consolidated depreciation and amortization	$ 898	$ 978	$ 1,854	$ 2,159

	As of June 30, 2011	As of December 31, 2010
Identifiable assets by segment:		
DIS	$ 13,976	$ 13,874
Product	38,810	38,547
Consolidated assets	$ 52,786	$ 52,421

Note 8. Income Taxes

As of December 31, 2010, the Company had unrecognized tax benefits of approximately $1.6 million. There has been no significant change in unrecognized tax benefits through June 30, 2011. Included in the unrecognized tax benefits of $1.6 million at December 31, 2010 was $1.4 million of tax benefits that, if recognized, would reduce the Company s annual effective tax rate, subject to the valuation allowance. The Company does not expect its unrecognized tax benefits to change significantly over the next 12 months.

The Company files income tax returns in the U.S. and in various state jurisdictions with varying statutes of limitations. The Company is no longer subject to income tax examination by tax authorities for years prior to 2006; however, its net operating loss and research credit carry-forwards arising prior to that year are subject to adjustment. The Company s policy is to recognize interest expense and penalties related to income tax matters as a component of income tax expense. There were no accrued interest and penalties associated with uncertain tax positions as of June 30, 2011 and December 31, 2010.

Note 9. Commitments and Contingencies

Stock Repurchase Program

On February 4, 2009, the Company s board of directors authorized a stock buyback program to repurchase up to an aggregate of $2.0 million of its issued and outstanding common shares. The timing and extent of the repurchase depends upon market conditions, applicable legal requirements, and other factors. During the three and six months ended June 30, 2011, the Company had not repurchased any shares of its common stock under the stock buyback program. Since the inception of the program, the Company has repurchased 573,218 shares of its common stock at a cost of $1.0 million, at a weighted average price of $1.79 per share.

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Legal Matters

In the normal course of business, the Company has been, and will likely continue to be, subject to litigation or administrative proceedings incidental to its business, such as claims related to customer disputes, employment practices, wage and hour disputes, product liability, professional liability, commercial disputes, licensure restrictions or denials, and warranty or patent infringement. Responding to litigation or administrative proceedings, regardless of whether they have merit, can be expensive and disruptive to normal business operations. As litigation and the administrative proceedings are inherently uncertain, the Company cannot predict the outcome of such matters. While the ultimate outcome of litigation is always uncertain, the Company does not believe that it will have a material adverse effect on its business or financial results.

ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis should be read in conjunction with our financial statements and notes thereto included in this report on Form 10-Q, and the audited financial statements and notes as of and for the year ended December 31, 2010 included in our Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 9, 2011. Operating results are not necessarily indicative of results that may occur in future periods.

This report contains various forward-looking statements regarding our business, financial condition, results of operations and future plans and projects. Forward-looking statements discuss matters that are not historical facts and can be identified by the use of words such as believes, expects, anticipates, estimates, can, could, may, will, would, might or similar expressions. In this report, for example, we make f statements regarding, among other things, our expectations about the rate of revenue growth in specific business segments and the reasons for that growth and our profitability, our expectations regarding an increase in sales, strategic traction and marketing and sales spending, uncertainties relating to our ability to compete, uncertainties relating to our ability to increase our market share, changes in coverage and reimbursement policies of the Center for Medicare and Medicaid Services along with third-party payers and the effect on our ability to sell our products and services, our ability to timely develop new products or services that will be accepted by the market, competition from alternative imaging modalities, declining average selling prices for our Product offerings, supplies of radiopharmaceuticals, and the profitability of our business.

Although these forward-looking statements reflect our good faith judgment, such statements can only be based upon facts and factors currently known to us. Forward-looking statements are inherently subject to risks and uncertainties, many of which are beyond our control. As a result, our actual results could differ materially from those anticipated in these forward-looking statements as a result of various factors, including those set forth below under the caption Risk Factors. For these statements, we claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995. You should not unduly rely on these forward-looking statements, which speak only as of the date on which they were made. They give our expectations regarding the future, but are not guarantees. We undertake no obligation to update publicly or revise any forward-looking statements, whether as a result of new information, future events or otherwise, unless required by law.

Overview

We are a leading developer and manufacturer of medical diagnostic imaging systems including solid-state gamma cameras for nuclear cardiology and general nuclear medicine applications. We also are one of the largest national providers of in-office nuclear cardiology imaging and ultrasound services to physician practices, hospitals and imaging centers through our Digirad Imaging Solutions (DIS) business segment. We designed and commercialized the first solid-state nuclear gamma camera for the detection of cardiovascular disease and other medical conditions. Our imaging systems are sold in both portable and fixed configurations, and provide enhanced operability, improved patient comfort and, in the case of our triple-headed Cardius® 3 XPO system, shorter image acquisition time when compared to traditional vacuum tube cameras or our single or dual headed cameras. Our nuclear cameras fit easily into floor spaces as small as seven feet by eight feet and facilitate the delivery of nuclear medicine procedures in a physician s office, an outpatient hospital setting or within multiple departments of a hospital.

Our Business Segments

We generate revenues within two primary operating segments: our DIS segment (our personnel and equipment leasing service business) and our Product segment (the manufacture and sales of our medical diagnostic camera business).

Our DIS Segment. Through DIS, we offer a comprehensive personnel and equipment leasing services program as an alternative to purchasing a gamma camera or ultrasound equipment for physicians who wish to perform nuclear imaging, echocardiography, vascular ultrasound, or any

combination of these procedures in their offices by leasing the imaging system, certified personnel and other support required to perform imaging in the physician s office. The flexibility of our products and our DIS leasing service allows physicians more control over the diagnosis and treatment of their patients in their offices and to retain revenue from procedures they would otherwise refer elsewhere. DIS leasing services are primarily provided to cardiologists, internal medicine physicians and family practice doctors who enter into annual contracts for personnel and equipment services delivered on a per-day basis. Our typical lease contracts provide service coverage ranging from once per month to five times per week. We experience some seasonality in our DIS business related to vacations, holidays and inclement weather.

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Our Product Segment. Our Product revenue results primarily from selling solid-state gamma cameras and camera maintenance contracts. We sell our imaging systems to physician offices, hospitals, and imaging centers primarily in the United States, although we have sold a small number of imaging systems internationally. In order to address an industry need for an attenuation correction solution and as part of our product roadmap, we introduced a new product in 2009 called our Cardius® X-ACT camera, which is a rapid cardiac SPECT/VCT imager. The Cardius® X-ACT camera is positioned toward the hospital market and larger cardiology practices. In 2010, we expanded our product line further and introduced our new ergo general purpose portable imaging system, which is also targeted to hospital customers. Our nuclear gamma cameras are designed to create images of the inside of a patient s body using radioactive isotopes. The ergo system can be easily moved around inside the hospital so patients who cannot be taken to a nuclear medicine department can still be scanned. It includes a detector with a 12.5-inch-by-15.5-inch field of view, which is large enough to scan lungs and other organs larger than the heart. It is our first nuclear imaging camera not exclusively focused on cardiology. We believe our ergo imaging system will allow us to expand into new and growing market segments.

Our Market

The target market for our products and services includes cardiologists, internal medicine physicians, family practice physicians, imaging centers and hospitals in the United States that perform or could perform nuclear cardiac and ultrasound procedures. As of June 30, 2011, we provide imaging services through DIS to more than 1,100 physicians and physician groups. We have sold over 670 cameras through our Product segment. More than half of our DIS nuclear and ultrasound imaging customers are internal medicine physicians or other primary care practitioners, and the remainder are primarily cardiologists. Our market has been negatively affected, particularly in 2010, by lower physician reimbursements from the Center for Medicare and Medicaid Services (CMS) and third party providers for the codes under which our physician customers bill for our services, pricing pressures, decreases in radiopharmaceutical isotope supplies and continuing efforts by some third party payers to reduce health care expenditures by requiring physicians to obtain specific accreditations or certifications. We have been addressing and will continue to address these market pressures by introducing new products, modifying our DIS business model, and assisting our physician customers in complying with new regulations and requirements. We anticipate introducing other new products and services in 2011 and beyond.

Trends and Drivers

The medical device industry, including the market for nuclear and ultrasound imaging systems and services, is highly competitive. Our business continues to be affected by many factors, including generally declining healthcare reimbursement rates for cardiac imaging procedures (although reimbursement for nuclear imaging increased in 2011, it did not offset the declines in 2010), competition from alternative imaging modalities such as positron emission tomography (PET) and computed tomography (CT) angiography, competition from other small owner-operated mobile nuclear imaging providers, declining average selling prices for our product offerings and general uncertainty in the healthcare marketplace. We continue to experience significant market changes due to the decline in reimbursement rates and the uncertainty with healthcare legislation. We also continue to experience lower demand for our cameras, partially due to very limited hospital and physician group capital budgets and the general downturn in the economy. We expect most of these trends to continue in the foreseeable future.

In our DIS segment, our physician customers experienced a significant decrease in reimbursement in 2010 from CMS and third party providers for the codes under which our physician customers bill for our services. This decrease caused our physician customer to complete fewer scans in their office which reduced the volume of our service and forced us to reduce the pricing for our services. The challenges of 2010 have eased considerably and reimbursements for 2011 have actually increased. Furthermore, the worldwide medical radiopharmaceutical shortage that reduced the number of our scan days in 2010 is over and the supply appears to be restored. The uncertainty over the enactment of future legislation that may impact reimbursement rates continues to linger and cause concern with our physician customers. Congress is expected to address this issue before the end of the year. We continue to modify our business model in order to adapt to environmental and regulatory changes in our dynamic healthcare marketplace.

In our Product segment, we continue to build on past Product segment achievements by introducing new products targeted specifically at the larger physician practices and hospital marketplace. Our target market for our Product segment is shifting with a heavier focus toward the hospital market with the introduction of our Cardius® X-ACT camera and our ergo general purpose portable imaging system. In 2009, we received U.S. Food and Drug Administration (FDA) 510(k) clearance for our Cardius® X-ACT imaging system. In 2010, we introduced our new ergo general purpose portable imaging system. We believe that our product mix will begin to reflect more ergo general purpose portable imaging system sales as we penetrate the hospital marketplace. Although the hospital sales cycles tend to be longer than the in-office market sales cycles, we have already sold and installed several ergo imaging systems into leading U.S. hospitals and expect that trend to accelerate.

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First Six months of 2011 Financial Highlights

Our consolidated revenues were $28.4 million for the six months ended June 30, 2011, which represented an increase of $0.2 million, or 0.7%, over the comparable prior year period. DIS revenue decreased $1.0 million, or 4.7%, primarily due to a reduction in the number of days we were able to scan for our physician customers. The number of scan days was reduced due to the severe weather in the Midwest and East in January and February 2011 in addition to other business factors such as physician pre-certification requirements which makes it more difficult for our physician customers to utilize our services. Product revenues for the six months ended June 30, 2011 increased by $1.2 million, or 15.0%, compared to the prior year period, primarily due to a larger number of new cameras (compared to used cameras) sold to cardiology practices and hospitals. Our ergo system represented the majority of our cameras sold in the period.

We realized a significantly lower net loss for the six months ended June 30, 2011, compared to the same six month period in 2010. Our consolidated net loss for the six months ended June 30, 2011 was $0.6 million, compared to a net loss of $4.3 million during the same period in the prior year. The increase in gross profit of our DIS segment was primarily attributable to an improvement in labor and equipment utilization. The increase in gross profit of our Product segment was primarily attributable to sales of our new ergo general purpose portable nuclear imaging system, which yielded a higher average selling price than the cameras sold in the prior year same period.

Our DIS business currently operates in 19 states. For the six months ended June 30, 2011, DIS operated 64 nuclear gamma cameras and 68 ultrasound imaging systems, compared to 66 nuclear gamma cameras and 65 ultrasound imaging systems during the same period in the prior year. The decrease in nuclear gamma cameras was primarily due to a decline in the number of days our customers needed our services and our desire to maximize utilization of our equipment. We are seeking to improve our overall profitability through more efficient utilization of our fleet of gamma cameras and ultrasound equipment. In some cases, we use cameras as back-up cameras (which reside at our various hub locations and are used when primary cameras are in need of repair); and in other cases, we sell or move our cameras to fixed site customer locations. We measure efficiency by tracking system utilization, which is measured based on the percentage of days that our nuclear gamma cameras and ultrasound equipment are used to deliver services to customers out of the total number of days that they are available to deliver such services. System utilization decreased to 58.1% for the six months ended June 30, 2011, compared to 62.1% during the same period in the prior year, primarily due to fewer scan days as discussed above.

Results of Operations

The following table sets forth our results from operations expressed as percentages of revenues for the three and six months ended June 30, 2011 and 2010:

	Three Months Ended June 30,					
	2011	% of 2011 Revenues	2010	% of 2010 Revenues	Change from Prior Year Dollars	Change from Prior Year Percent
Revenues:						
DIS	$ 9,950	69.8%	$ 9,787	74.4%	$ 163	1.7%
Product	4,299	30.2%	3,372	25.6%	927	27.5%
Total revenues	14,249	100%	13,159	100%	1,090	8.3%
Total cost of revenues	10,255	72.0%	11,251	85.5%	(996)	(8.9)%
Gross profit	3,994	28.0%	1,908	14.5%	2,086	109.3%
Operating Expenses:						
Research and development	714	5.0%	870	6.6%	(156)	(17.9)%
Marketing and sales	1,617	11.3%	1,551	11.8%	66	4.3%
General and administrative	1,866	13.1%	2,139	16.3%	(273)	(12.8)%
Amortization of intangible assets	83	0.6%	107	0.8%	(24)	(22.4)%
Restructuring loss		0.0%	352	2.7%	(352)	(100.0)%
Total operating expenses	4,280	30.0%	5,019	38.1%	(739)	(14.7)%

Loss from operations	(286)	(2.0)%	(3,111)	(23.6)%	2,825	(90.8)%
Other income	58	0.4%	27	0.2%	31	114.8%
Net loss	$ (228)	(1.6)%	$ (3,084)	(23.4)%	$ 2,856	(92.6)%

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	Six months Ended June 30,					
	2011	% of 2011 Revenues	2010	% of 2010 Revenues	Change from Prior Year Dollars	Change from Prior Year Percent
Revenues:						
DIS	$ 19,546	68.8%	$ 20,509	72.7%	$ (963)	(4.7)%
Product	8,878	31.2%	7,718	27.3%	1,160	15.0%
Total revenues	28,424	100%	28,227	100%	197	0.7%
Total cost of revenues	20,910	73.6%	22,948	81.3%	(2,038)	(8.9)%
Gross profit	7,514	26.4%	5,279	18.7%	2,235	42.3%
Operating Expenses:						
Research and development	1,422	5.0%	1,595	5.7%	(173)	(10.8)%
Marketing and sales	3,041	10.7%	3,181	11.3%	(140)	(4.4)%
General and administrative	3,970	14.0%	4,400	15.6%	(430)	(9.8)%
Amortization of intangible assets	176	0.6%	239	0.8%	(63)	(26.4)%
Restructuring (gain) loss	(164)	(0.6)%	352	1.2%	(516)	(146.6)%
Total operating expenses	8,445	29.7%	9,767	34.6%	(1,322)	(13.5)%
Loss from operations	(931)	(3.3)%	(4,488)	(15.9)%	3,557	(79.3)%
Other income	317	1.1%	169	0.6%	148	87.6%
Net loss	$ (614)	(2.2)%	$ (4,319)	(15.3)%	$ 3,705	(85.8)%

Comparison of Three Months Ended June 30, 2011 and 2010

Revenues

Consolidated. Consolidated revenue was $14.2 million for 2011, an increase of $1.1 million, or 8.3%, compared to the prior year quarter, primarily as a result of an increase in the number of camera sales in our Product business segment. DIS revenue accounted for 69.8% of total revenues for 2011, compared to 74.4% for the prior year quarter. Although we expect our Product revenue to continue to grow, we also expect our DIS revenue to continue to represent the larger percentage of our consolidated revenue.

DIS. Our DIS revenue was $10.0 million for the three months ended June 30, 2011, an increase of $0.2 million, or 1.7%, compared to the prior year quarter. The increase in 2011 resulted from an increase in the number of studies we performed in 2011 due to the availability of isotope supply combined with some additional contract revenue for providing compliance services.

Product. Our Product revenue was $4.3 million for the three months ended June 30, 2011, an increase of $0.9 million, or 27.5%, compared to the prior year quarter. The increase in revenue resulted from an increase in the number of gamma camera sales this year compared to the prior year quarter, mainly ergo system sales.

Cost of Revenue and Gross Profit

Consolidated. Consolidated gross profit was $4.0 million for the three months ended June 30, 2011, an increase of $2.1 million, or 109.3%, compared to the prior year quarter. The increase in consolidated gross profit is primarily the result of the increase in DIS and Product revenues compared to the prior year period as well as lower costs compared to the prior year period. Consolidated gross profit as a percentage of revenue increased to 28.0% for the three months ended June 30, 2011 from 14.5% for the prior year quarter.

DIS. Cost of DIS revenue consists primarily of labor, radiopharmaceuticals, equipment depreciation, and other costs associated with the provision of services. Cost of DIS revenue was $7.8 million for the three months ended June 30, 2011, a decrease of $0.4 million, or 4.9%, compared to the prior year quarter. The decrease in cost of DIS revenue is primarily a result of decreased expenses from a more efficient utilization of our labor and equipment. DIS gross profit was $2.2 million for the three months ended June 30, 2011, an increase of $0.6 million,

or 34.9%, from a gross profit of $1.6 million for the prior year quarter. DIS gross profit as a percentage of DIS revenue increased to 21.9% for the three months ended June 30, 2011 from 16.5% for the prior year quarter. The improvement in operational performance is primarily associated with the management of labor and equipment resources.

Product. Cost of Product revenue primarily consists of materials, labor and overhead costs associated with the manufacturing and warranty of our products. Cost of goods sold for the Product segment was $2.5 million for the three months ended June 30, 2011, a decrease of $0.6 million, or 19.4%, compared to the prior year quarter. The decrease in cost of Product revenue is primarily a result of higher production volumes, a change in the camera mix toward ergo systems and better cost management, partially offset by certain costs related to our new key component supplier.

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Product gross profit was $1.8 million for the three months ended June 30, 2011, an increase of $1.5 million, or 519.8%, compared to the prior year period. Product gross profit as a percentage of Product revenue increased to 42.2% for the three months ended June 30, 2011 compared to 8.7% for the prior year quarter, primarily due to increased camera sales and lower manufacturing variances, including but not limited to lower excess and obsolete reserves this year compared to last year.

Operating Expenses

Research and Development. Research and development expenses are the costs associated with the design, development and enhancement of our products, and consist of salaries, development material costs, facility and overhead costs, consulting fees, and non-recurring engineering costs. We continue to invest in research and development with a focus on innovation as we seek to improve our existing technology. In 2009 and 2010, we received U.S. Food and Drug Administration 510(k) clearance for our new Cardius® X-ACT imaging system and ergo general purpose portable imaging system, respectively. Research and development expenses were $0.7 million for the three months ended June 30, 2011, a decrease of $0.2 million, or 17.9%, compared to the prior year quarter, primarily as a result of 2010 research and development efforts (including clinical evaluation expenses) for the previously mentioned cameras, which did not reoccur in 2011. Research and development expenses were 16.6% of Product revenue for the three months ended June 30, 2011 compared to 25.8% in the prior year quarter, a decrease of 9.2%. We plan to continue investing in our technology platform to penetrate new and existing market segments and attract new customers.

Marketing and Sales. Marketing and sales expenses consist primarily of salaries, commissions, bonuses, recruiting costs, travel, marketing and collateral materials and trade show costs. Marketing and sales expenses were $1.6 million for the three months ended June 30, 2011, the same amount compared to the prior year quarter. Marketing and sales expenses as a percentage of total revenues were 11.3% varying slightly from 11.8% for the three months ended June 30, 2011 and 2010, respectively.

General and Administrative. General and administrative expenses consist primarily of salaries and other related costs for accounting, human resources, information technology and executive personnel, legal related costs, professional fees, outside services, insurance, and costs related to our board of directors. General and administrative expenses were $1.9 million for the three months ended June 30, 2011, a decrease of $0.3 million, or 12.8%, compared to the prior year quarter. This decrease is primarily the result of lower bad debt reserves and lower legal and consulting services compared to the prior year period. General and administrative expenses were 13.1% of total revenue for the three months ended June 30, 2011 compared to 16.3% for the prior year quarter, mainly due to higher Product revenue in 2011.

Restructuring Loss

In response to continued changing market conditions, which contributed to operating losses within our DIS and Product business segments, we reduced our workforce during the second quarter of 2010. We incurred restructuring charges of approximately $0.4 million in the second quarter of 2010, which included severance payments of approximately $0.2 million, write-offs of excess cameras and capital equipment of approximately $0.2 million and other related costs. There were no comparable costs incurred in the second quarter of 2011.

Comparison of Six months Ended June 30, 2011 and 2010

Revenues

Consolidated. Consolidated revenue was $28.4 million for six months ended June 30, 2011, an increase of $0.2 million, or 0.7%, compared to the prior year, primarily as a result of an increase in revenue from our Product segment from higher camera sales, partially offset with decreased DIS segment revenue. DIS revenue accounted for 68.8% of total revenues for 2011, compared to 72.7% for the prior year. We expect DIS revenue to continue to represent the larger percentage of our consolidated revenue.

DIS. Our DIS revenue was $19.5 million for the six months ended June 30, 2011, a decrease of $1.0 million, or 4.7%, compared to the prior year. The decrease resulted from a reduction in the number of days we were able to scan for our physician customers. The number of scan days was reduced partially due to the severe weather in the Midwest and East in January and February 2011 and partially due to other environmental factors such as physician pre-certification requirements.

Product. Our Product revenue was $8.9 million for the six months ended June 30, 2011, an increase of $1.2 million, or 15.0%, compared to the prior year. The increase in revenue was primarily due to a higher number of new cameras (compared to used cameras) sold, mainly our new ergo system.

Cost of Revenue and Gross Profit

Consolidated. Consolidated gross profit was $7.5 million for the six months ended June 30, 2011, increase of $2.2 million, or 42.3%, compared to the prior year. The increase in consolidated gross profit is primarily the result of improving gross margins in DIS due to lower labor costs during the six months ended June 30, 2011 in addition to increased Product revenue primarily due to a higher number of cameras sold. Consolidated gross profit as a percentage of revenue increased to 26.4% for the six months ended June 30, 2011 from 18.7% for the prior year.

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DIS. Cost of DIS revenue consists primarily of labor, radiopharmaceuticals, equipment depreciation, and other costs associated with the provision of services. Cost of DIS revenue was $15.5 million for the six months ended June 30, 2011, a decrease of $1.4 million, or 8.5%, compared to the prior year. The decrease in cost of DIS revenue is primarily a result of decreased expenses from fewer scans and also from more efficient utilization of labor and equipment. DIS gross profit was $4.0 million for the six months ended June 30, 2011, which represents an increase of $0.5 million, or 13.5%, from a gross profit of $3.5 million for the prior year. DIS gross profit as a percentage of DIS revenue increased to 20.5% for the six months ended June 30, 2011 from 17.2% for the prior year due to improvement in operational performance primarily associated with the management of labor and equipment resources.

Product. Cost of Product revenue primarily consists of materials, labor and overhead costs associated with the manufacturing and warranty of our products. Cost of revenues for the Product segment was $5.4 million for the six months ended June 30, 2011, a decrease of $0.6 million, or 10.0%, compared to the prior year. The stability in cost of Product revenue is primarily a result of higher production volumes, a change in the camera mix toward ergo systems and better cost management, partially offset by certain costs related to our new key component supplier. Product gross profit was $3.5 million for the six months ended June 30, 2011, an increase of $1.8 million, or 100.8%, compared to the prior year period. Product gross profit as a percentage of Product revenue increased to 39.4% for the six months ended June 30, 2011 compared to 22.6% for the prior year, primarily due to the mix of new versus used cameras sold.

Operating Expenses

Research and Development. Research and development expenses are the costs associated with the design, development and enhancement of our products, and consist of salaries, development material costs, facility and overhead costs, consulting fees, and non-recurring engineering costs. We continue to invest in research and development with a focus on innovation as we seek to improve our existing technology. In 2009 and 2010, we received U.S. Food and Drug Administration 510(k) clearance for our new Cardius® X-ACT imaging system and ergo general purpose portable imaging system, respectively. Research and development expenses were $1.4 million for the six months ended June 30, 2011, a decrease of $0.2 million, or 10.8%, compared to the prior year primarily as a result of 2010 research and development efforts (including clinical evaluation expenses) for the previously mentioned cameras, which did not reoccur in 2011. Research and development expenses were 16.0% of Product revenue for the six months ended June 30, 2011 compared to 20.7% in the prior year, a decrease of 4.7%. We plan to continue investing in our technology platform to penetrate new and existing market segments, support new product introductions and attract new customers.

Marketing and Sales. Marketing and sales expenses consist primarily of salaries, commissions, bonuses, recruiting costs, travel, marketing and collateral materials and trade show costs. Marketing and sales expenses were $3.0 million for the six months ended June 30, 2011, a decrease of $0.1 million, or 4.4%, compared to the prior year, primarily as a result of lower sales commissions paid due to lower DIS sales volume. Marketing and sales expenses as a percentage of total revenues were 10.7% varying slightly from 11.3% for the six months ended June 30, 2011 and 2010, respectively.

General and Administrative. General and administrative expenses consist primarily of salaries and other related costs for accounting, human resources, information technology and executive personnel, legal related costs, professional fees, outside services, insurance, and costs related to our board of directors. General and administrative expenses were $4.0 million for the six months ended June 30, 2011, a decrease of $0.4 million, or 9.8%, compared to the prior year. This decrease is primarily the result of lower bad debt reserves and lower legal and consulting services compared to the prior year period. General and administrative expenses were 14.0% of total revenue for the six months ended June 30, 2011 compared to 15.6% for the prior year.

Restructuring (Gain) Loss. In 2009, we financed a note receivable related to certain assets that we sold as part of our restructuring efforts. We fully reserved the note at that time. The buyer recently paid the note in full and we recognized a $0.2 million gain on the transaction in the first quarter of 2011.

In response to continued changing market conditions, which contributed to operating losses within our DIS and Product business segments, we reduced our workforce during the second quarter of 2010. We incurred restructuring charges of approximately $0.4 million in the second quarter of 2010, which included severance payments of approximately $0.2 million, write-offs of excess cameras and capital equipment of approximately $0.2 million and other related costs.

Liquidity and Capital Resources

We require working capital principally to finance accounts receivable and inventory and for capital expenditures. Our working capital requirements vary from period to period depending on several factors, including our manufacturing volumes, the timing of our deliveries and the payment cycles of our customers. Our capital expenditures consist primarily of DIS nuclear cameras, ultrasound equipment, and vans to transport our people and equipment to customer locations.

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As of June 30, 2011, we had cash, cash equivalents and securities available-for-sale of $31.1 million. We currently invest our cash reserves in money market funds as well as U.S. treasury and corporate debt securities. Based upon our current level of expenditures, we believe our current working capital, together with cash flows from operating activities, will be more than adequate to meet our anticipated cash requirements for working capital, debt service and capital expenditures for at least the next 12 months.

Cash Flows

The following table shows cash flow information for the six months ended June 30, 2011 and 2010 (in thousands):

	Six months Ended June 30,	
	2011	**2010**
Net cash provided by (used in) operating activities	$ 1,370	$ (623)
Net cash (used in) provided by investing activities	(12,439)	1,918
Net cash used in financing activities	(21)	(40)

Operating Activities

Net cash provided by operating activities increased $2.0 million, or 319.9%, for the six months ended June 30, 2011 compared to the prior year period. This increase was primarily attributable to our decreased net loss partially offset by changes in working capital.

Investing Activities

Net cash used in investing activities increased $14.3 million, or 748.5%, for the six months ended June 30, 2011 compared to the prior year period. This increase was primarily attributable to purchases of securities available for sale partially offset by fewer maturities of securities available-for-sale and capital expenditures during the six months ended June 30, 2011.

Financing Activities

Net cash used in financing activities decreased by less than $0.1 million, or 47.5%, for the six months ended June 30, 2011 compared to the prior year period. This decrease was primarily attributable to no repurchases of common stock during the six months ended June 30, 2011.

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Critical Accounting Policies

Management s discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements which are prepared in accordance with accounting principles that are generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets and liabilities, related disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. We continually evaluate our estimates and judgments, the most critical of which are those related to revenue recognition and inventory valuation. We base our estimates and judgments on historical experience and other factors that we believe to be reasonable under the circumstances. Materially different results can occur as circumstances change and additional information becomes known. The accounting policies are the same as those described in the critical accounting policies in our Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 9, 2011.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our exposure to market risk due to changes in interest rates relates primarily to the increase or decrease in the value of debt securities in our investment portfolio. Our risk associated with fluctuating interest rates is limited to our investments in interest rate sensitive financial instruments. Under our current policies, we do not use interest rate derivative instruments to manage exposure to interest rate changes. We attempt to increase the safety and preservation of our invested principal funds by limiting default risk, market risk and reinvestment risk. We mitigate default risk by investing in investment grade securities. A 100 basis point adverse move in interest rates along the entire interest rate yield curve would not materially affect the fair value of our interest sensitive financial instruments. Changes in interest rates over time will increase or decrease our interest income.

ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

We maintain disclosure controls and procedures and internal controls that are designed to provide reasonable assurance that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission s rules and forms and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures and internal controls, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable, and not absolute, assurance of achieving the desired control objectives. In reaching a reasonable level of assurance, management necessarily is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures and internal controls.

As required by the Securities and Exchange Commission Rule 13a-15(e) and Rule 15d-15(e), we carried out an evaluation, under the supervision of and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this report. Based on the foregoing, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective at the reasonable assurance level.

Changes in Internal Control over Financial Reporting

There have been no changes in our internal control over financial reporting during the second quarter of fiscal 2011 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

In the normal course of business, we have been, and will likely continue to be, subject to litigation or administrative proceedings incidental to our business, such as claims related to customer disputes, employment practices, wage and hour disputes, product liability, professional liability,

commercial disputes, licensure restrictions or denials, and warranty or patent infringement. Responding to litigation or administrative proceedings, regardless of whether they have merit, can be expensive and disruptive to normal business operations. As litigation and the administrative proceedings are inherently uncertain, we cannot predict the outcome of such matters. While the ultimate outcome of litigation is always uncertain, we do not believe that it will have a material adverse effect on our business or financial results.

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ITEM 1A. RISK FACTORS

There have been no material changes to the Risk Factors described under Part I Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2010 filed with the Securities and Exchange Commission on March 9, 2011, other than:

- removal of the risk factor entitled Failure to retain qualified technologists could limit our growth and adversely affect our business;
- changes to the risk factor below entitled Our manufacturing operations are highly dependent upon the availability of certain third-party suppliers, thereby making us vulnerable to supply problems that could harm our business, which has been updated to reflect the recent developments with one of our sole suppliers of a key component of our gamma cameras.

Risks Related to Our Business and Industry

Our revenues may decline further due to reductions in Medicare reimbursement rates.

The success of our business is largely dependent upon our medical professional customers ability to provide diagnostic imaging care to their patients in an economically sustainable manner, either through the purchase of our imaging systems or using our lease services, or both. Our customers are directly impacted by changes (decreases and increases) in governmental and private payor reimbursements for diagnostic imaging. Although we are not directly impacted by changes in reimbursements, we make every effort to act as business partners with our physician customers, e.g., in 2010, we proactively adjusted the fair market value of our personnel and equipment leasing services rate due to the dramatic reimbursement declines that our customers were facing. Although Medicare/Medicaid reimbursement for the imaging modalities that we offer increased slightly in 2011 in the physician office setting, this occurred only after a significant decline in ultrasound reimbursements in 2009 (phased-in over the next four years) and a significant decline in nuclear reimbursements in 2010. Current reimbursement has not yet been restored to prior levels. Private payors often follow the lead of Medicare/Medicaid with respect to reimbursement criteria and payment levels. This causes greater pricing pressure on our lease services and also influences buying decisions of our individual physician Product customers. Hospital reimbursements, however, have remained higher and our newer imaging systems are better targeted to serve this expanding hospital market. Only a small portion of our DIS business segment operates in the hospital market.

Further cuts in reimbursements could significantly impact the viability of in-office imaging performed by independent physicians. The uncertainty surrounding this issue and the historical decline in reimbursements has resulted in cancellations of imaging days in our personnel and equipment lease services business and the delay of purchase and lease decisions by our existing and prospective customers in our Product sales business. Additional declines in Medicare/Medicaid reimbursement for our relevant diagnostic imaging modalities are possible due to the many factors, including but not limited to the threatened implementation of the federal sustainable growth factor (SGR). The SGR is part of the relative value unit (RVU), a formula that was enacted by Congress as part of the Balanced Budget Act of 1997 to control the cost of the Medicare program. It applies to all health services paid for by Medicare, not just diagnostic imaging. The application of the SGR has been delayed by Congress for many years and most recently, Congressional action has delayed it again until January 1, 2012. If Congress allows the SGR to go into effect in 2012, all Medicare codes could incur a reimbursement reduction of approximately 31%. Though Congressional leadership has said they will address this issue before the end of the year, there is no assurance the issue will be timely or favorably resolved, and if not favorably resolved, it could have a material adverse impact on our business.

Our revenues may decline further due to changes in diagnostic imaging regulations and use of third parties by private payors to drive down imaging volumes.

Nuclear medicine is a designated health service under the federal physician self-referral prohibition law known as the Stark Law, which states that a physician may not refer designated health services to an entity with which the physician or an immediate family member has a financial relationship, unless a statutory exception applies. Our business model and lease agreements are structured to enable our physician customers to meet the statutory *in-office ancillary services* (IOAS) exception to the Stark Law allowing them to perform nuclear diagnostic imaging services on their patients in the convenience of their own office. From time-to-time, the Centers for Medicare and Medicaid Services (CMS) and Congress have proposed to modify the IOAS to further limit or eliminate this exception. Various lobbying organizations are pushing for, and the Medicare Payment Advisory Commission (MedPAC) is actively discussing, limiting the availability of the IOAS exception in order to reduce federal healthcare costs. The outcome of these efforts and discussions is uncertain at this time; however, the limitation or elimination of the IOAS exception could significantly impact our DIS business segment as currently structured.

Our customers who perform imaging services in their office also experience the continuing efforts by some private insurance companies to reduce healthcare expenditures by hiring radiology benefit managers (RBM) to help them manage and limit imaging. The federal government

has also set aside monies in the 2009 recession recovery acts to hire RBM s to provide image management services to Medicare/Medicaid and MedPAC has recommended and CMS has proposed legislation requiring Medicare physicians who engage in a relatively high volume of medical imaging be required to obtain pre-authorization through an RBM. An RBM is an unregulated entity that performs various functions for private payors and managed care organizations depending on what they have

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been contracted to perform. RBM activities can include pre-authorization for imaging procedures, setting and enforcing standards approving which contracted physicians can perform the services, such as requiring even the most experienced and highly qualified cardiologists to obtain additional board certifications or interfering with the financial decision of the private practitioner by requiring them to own their own imaging system and not allowing them to lease the system. The RBM s often do not provide written documentation of their decisions or an appeals process, leaving leasing physicians unable to challenge RBM decisions with the carrier or the state insurance department. Some efforts are being made to address certain RBM issues, for example, the New York State Attorney General recently entered into a settlement requiring an RBM (based and operating in New York State) to buy out its owners in the state who own imaging centers because it created a conflict of interest in their decisions to deny authorization for competing physicians to provide imaging services; and, New York is requiring the RBM to establish an appeals process. However, unregulated RBM activities have and could continue to adversely affect our physician customers ability to receive reimbursement, therefore impacting our customers decision to utilize our DIS leasing services.

Our manufacturing operations are highly dependent upon the availability of certain third-party suppliers, thereby making us vulnerable to supply problems that could harm our business.

We rely on a limited number of third parties to manufacture and supply certain key components of our products. Alternative sources of production and supply may not be readily available or may take several months to scale-up and develop effective production processes. If a disruption in the availability of parts or in the operations of our suppliers were to occur, such as with respect to components manufactured in Japan, our ability to build gamma cameras could be materially affected. For this reason, we have backup plans in place that are designed to prevent delays in production. If these plans are unsuccessful, delays in the production of our gamma cameras for an extended period of time could cause a loss of revenue, which could significantly harm our business and results of operations.

In late 2010, the sole supplier of a key component of our new ergo gamma camera ceased production of a critical component. We have a very limited supply of that key component and are currently working with a new supplier who has already successfully provided the component. We are working with our new supplier to improve the yield, cost and efficiency of the key component, which efforts are expected to continue through Q1 of 2012. We are also expanding our supply relationships with other third party suppliers in order to minimize the reliance on one sole supplier. The process to qualify a supplier for this key component is long, complex and costly. If the key component is not available when we need it, it could adversely impact our production capability and therefore negatively impact our financial condition. Furthermore, lower yields on the manufacturing of the key component that we do receive from our supplier can have a negative impact on our financial condition through higher purchase price variances, which impact current period gross margins.

Our lease operations are highly dependent upon the availability of certain radiopharmaceuticals, thereby making us vulnerable to supply problems and price fluctuations that could harm our business.

Our personnel and equipment leasing service involves the use of radiopharmaceuticals. There were significant disruptions in the international supply of these radiopharmaceuticals in parts of 2009 and 2010, which caused us to cancel services that would have otherwise been provided and this adversely affected our financial condition in late 2009 and 2010. Although we now have supply, the two major nuclear reactors supplying medical radiopharmaceuticals worldwide came back on-line at the end of the third quarter of 2010 and we have developed a strong relationship with a radio pharmacy company, there is no guarantee that the reactors will remain in good repair and our supplier will have continuing access to ample supply of product. If we are unable to obtain an adequate supply of the necessary radiopharmaceuticals, we may be unable to lease our personnel and equipment through our in-office service operations, or the volume of our services could decline and our business may be adversely affected. Shortages can also cause price increases that may not be accounted for in third party reimbursement rates, thereby causing us to lose margin or require us to pass increases on to our physician customers.

Our business is not widely diversified.

Although we have a strategic initiative to expand our product line into general nuclear imaging with our ergo imaging system, which is primarily geared toward the hospital marketplace; historically, we have sold our products and leased our imaging systems and personnel primarily into the cardiac nuclear and ultrasound imaging private practice markets. We may not be able to leverage our assets and technology to diversify our products and services in order to generate revenue beyond the cardiac nuclear and ultrasound imaging private practice markets. If we are unable to diversify our product and service offerings, our financial condition may suffer.

We compete against businesses that have greater resources and different competitive strengths.

The market for cardiac nuclear imaging cameras is limited and has been decreasing. Our competition has greater resources and a more diverse product offering than we do. Some of our competitors enjoy significant advantages over us, including greater name recognition, greater financial and technical resources, established relationships with healthcare professionals, larger distribution networks, and greater resources for product

development, as well as more extensive marketing and sales resources. Additionally, certain medical device companies have developed alternative portable cameras that directly compete with our product offerings. If we are unable to expand our current market share, our revenues could decline.

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In addition, our personnel and equipment leasing services customers may switch to other service providers. Our personnel and equipment leasing services segment competes against small local, owner operated or regional businesses, some of whom have the advantage of a lower cost structure, and against imaging centers that install nuclear gamma cameras and make them available to physicians in their geographic vicinity. If these competitors are able to win significant portions of our business, our sales could decline significantly. Our financial condition could be adversely affected under such circumstances.

Our quarterly and annual financial results are difficult to predict and are likely to fluctuate from period to period.

We have historically experienced seasonality in our personnel and equipment leasing services business, and recent volatility due to the changing health care environment, the variable supply of radio-pharmaceuticals, and the downturn in the U.S. economy. While our physicians are obligated to pay us for all lease days to which they have committed, our contracts permit some flexibility in scheduling when services are to be performed. We cannot predict with certainty the degree to which seasonal circumstances such as the summer slowdown, winter holiday vacations and weather conditions may affect the results of our operations. We have also experienced fluctuations in demand of our cardiac nuclear gamma cameras due to economic conditions, capital budget availability, or other financial or business reasons. In addition, due to the way that customers in our target markets acquire our products, a large percentage of our camera orders are booked during the last month of each quarterly accounting period. As such, a delivery delay of only a few days may significantly impact our quarter-to-quarter comparisons. Moreover, the sales cycle in our Product segment for cameras is typically lengthy, particularly with our recent entry into the hospital market, which may cause us to experience significant revenue fluctuations. For these reasons, quarterly and annual sales and operating results may vary in the future. Therefore, period-to-period comparisons of our results of operations are not necessarily meaningful and should not be relied upon as indicators of future performance.

Our common stock is thinly traded and our options plan could affect the trading price of our common stock.

Our common stock is thinly traded and any significant sales of our common stock may cause volatility in our common stock price. We also have registered shares of common stock that we may issue under our employee benefit plans or from our treasury stock. Accordingly, these shares can be freely sold in the public market upon issuance, subject to restrictions under the securities laws. If any of these stockholders cause a large number of securities to be sold in the public market, the sales could reduce the trading price of our common stock. Although we are only aware of two single stockholders owning more than 4.99% of our stock and no one owning more than 14.99% of our stock, one or more stockholders holding a significant amount of our common stock might be able to significantly influence matters requiring approval by our stockholders, possibly including the election of directors and the approval of mergers or other business combination transactions.

We spend considerable time and money complying with federal and state laws, regulations and other rules, and if we are unable to comply with such laws, regulations and other rules, we could face substantial penalties.

We are directly, or indirectly through our physician customers, subject to extensive regulation by both the federal government and the states in which we conduct our business, including: the federal Medicare and Medicaid anti-kickback laws and other Medicare laws, regulations, rules, manual provisions, and policies that prescribe the requirements for coverage and payment for services performed by us and our physician customers; the federal False Claims statutes; the federal Health Insurance Portability and Accountability Act of 1996, or HIPAA, as amended in 2009 under the HITECH Act that places direct legal obligations and higher liability on us with respect to the security and handling of personal health information; the Stark Law; the federal Food, Drug and Cosmetic Act; federal and state radioactive materials laws; state food and drug and pharmacy laws and regulations; state laws that prohibit the practice of medicine by non-physicians and fee-splitting arrangements between physicians and non-physicians; state scope-of-practice laws; and federal rules prohibiting the mark-up of diagnostic tests to Medicare under certain circumstances. If our physician customers are unable or unwilling to comply with these statutes, regulations, rules, and policies, utilization rates of our services and products could decline and our business could be harmed. Additionally, new government mandates will require us to provide a certain baseline of health benefits and premium contribution for our employees and their families or pay governmental penalties. Some of these costs are not tax deductible. We have opted to provide this coverage to our employee base in order to maintain retention of qualified medical technicians and other professionals rather than plan to pay penalties to the government. Either option will result in additional costs to us and could negatively impact our cash reserves.

We maintain a compliance program to identify and correct any compliance issues and remain in compliance with all applicable laws, to train employees, to audit and monitor our operations, and to achieve other compliance goals. Like most companies with compliance programs, we occasionally discover compliance concerns. In such cases, we take responsive action including corrective measures when necessary. There can be no assurance that our responsive actions will insulate us from liability associated with any detected compliance concerns.

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If our past or present operations are found to be in violation of any of the laws, regulations, rules, or policies described above or the other laws or regulations to which we or our customers are subject, we may be subject to civil and criminal penalties, damages, fines, exclusion from federal or state health care programs, or the curtailment or restructuring of our operations. Similarly, if our physician customers are found to be non-compliant with applicable laws, they may be subject to sanctions which could have a negative impact on us. Any penalties, damages, fines, curtailment or restructuring of our operations could adversely affect our ability to operate our business and our financial results. Any action against us for violation of these laws, even if we successfully defend against it, could cause us to incur significant legal expenses, divert our management s attention from the operation of our business, and damage our reputation.

Our manufacturing operations and executive offices are located at a single facility that may be at risk from fire, earthquakes or other disasters.

Our manufacturing operations, research and development activities and executive offices are located in a single facility in Poway, California, near known fire areas and earthquake fault zones. Any future natural disaster could cause substantial delays in our Product operations, damage to our manufacturing equipment, research and development efforts and inventory, and cause us to incur additional expenses. Although we have taken precautions to insure our facilities and continuing operations, as well as provide for offsite back-up of our information systems, this may not be adequate to cover our losses in any particular case. A disaster could significantly harm our business and results of operations.

The medical device industry is litigious, which could result in the diversion of our management s time and efforts, and require us to pay damages which may not be covered by our insurance.

Our operations entail risks of claims or litigation relating to product liability, radioactive contamination, patent infringement, trade secret disclosure, warranty claims, product recalls, property damage, misdiagnosis, personal injury, and death. Any litigation or claims against us, or claims we bring against others, may cause us to incur substantial costs, could place a significant strain on our financial resources, divert the attention of our management from our core business and harm our reputation. We may incur significant liability in the event of any such litigation, regardless of the merit of the action. If we are unable to obtain insurance, or if our insurance is inadequate to cover claims, our cash reserves and other assets could be negatively impacted. Additionally, costs associated with maintaining our insurance could become prohibitively expensive, and our ability to become or remain profitable could be diminished.

Our ability to protect our intellectual property and proprietary technology through patents and other means is uncertain.

Our success depends, in part, on our ability to protect our proprietary rights to the technologies used in our products. Our pending United States patent applications, which include claims to material aspects of our products and procedures that are not currently protected by issued patents, may not issue as patents in a form that will be advantageous to us. Any patents we have obtained or do obtain may be challenged by re-examination or otherwise invalidated or eventually found unenforceable. Both the patent application process and the process of managing patent disputes can be time consuming and expensive. Competitors may attempt to challenge or invalidate our patents, or may be able to design alternative techniques or devices that avoid infringement of our patents, or develop products with functionalities that are comparable to ours. In the event a competitor infringes upon our patent or other intellectual property rights, litigation to enforce our intellectual property rights or to defend our patents against challenge, even if successful, could be expensive and time consuming and could require significant time and attention from our management. We may not have sufficient resources to enforce our intellectual property rights or to defend our patents against challenges from others.

Anti-takeover provisions in our organizational documents, our Stockholders Rights Plan and Delaware law may prevent or delay removal of current management or a change in control.

Our restated certificate of incorporation and restated bylaws contain provisions that may delay or prevent a change in control, discourage bids at a premium over the market price of our common stock, and adversely affect the market price of our common stock and the voting and other rights of the holders of our common stock. The rights issued pursuant to our Stockholder Rights Plan will become exercisable, subject to certain exceptions, the tenth day after a person or group announces acquisition of 20% or more of our common stock or announces commencement of a tender or exchange offer, the consummation of which would result in ownership by the person or group of 20% or more of our common stock. In addition, as a Delaware corporation, we are subject to Delaware law, including Section 203 of the Delaware General Corporation Law. In general, Section 203 prohibits a Delaware corporation from engaging in any business combination with any interested stockholder for a period of three years following the date that the stockholder became an interested stockholder unless certain specific requirements are met as set forth in Section 203. These provisions, alone or together, could have the effect of deterring or delaying changes in incumbent management, proxy contests or changes in control.

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ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

On February 4, 2009, our Board of Directors approved a stock repurchase program whereby we may, from time to time, purchase up to $2.0 million worth of our common stock in the open market, in privately negotiated transactions or otherwise, at prices that we deem appropriate. The plan has no expiration date. Details of purchases made during the years ended December 31, 2009, 2010 and the six months ended June 30, 2011 are as follows:

	Total Number of Shares Purchased During the Period	Average Price Paid Per Share for Period Presented	Total Cumulative Number of Shares Purchased as Part of Publicly Announced Plan	Maximum Dollar Value of Shares that May Yet Be Purchased Under the Plan
Period:				
February 4, 2009 February 28, 2009	8,700	$ 0.98	8,700	$ 1,991,474
March 1, 2009 June 30, 2009	2,600	0.99	11,300	1,988,900
May 1, 2009 May 31, 2009	183,500	1.26	194,800	1,758,352
June 1, 2009 September 30, 2009	14,300	1.25	209,100	1,740,438
July 1, 2009 July 31, 2009	33,200	2.14	242,300	1,669,307
August 1, 2009 August 31, 2009	192,918	2.02	435,218	1,279,640
September 1, 2009 September 30, 2009	14,000	2.11	449,218	1,250,085
November 1, 2009 November 30, 2009	93,200	2.28	542,418	1,037,627
December 1, 2009 December 31, 2009	5,000	2.38	547,418	1,025,739
February 1, 2010 February 28, 2010	25,800	1.91	573,218	976,571
As of June 30, 2011:	573,218	$ 1.79	573,218	$ 976,571

In addition to the above purchases, John Sayward, a member of our board of directors and an affiliated purchaser as defined in Rule 10b-18(a)(3), purchased 20,000 shares of common stock in the open market at an average price of $1.02 per share in February 2009.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. (REMOVED AND RESERVED)

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

Exhibit Number	Description
3.1(1)	Restated Certificate of Incorporation
3.2(2)	Restated Bylaws

4.1(3)	Form of Specimen Stock Certificate
4.2(4)	Amended and Restated Investors Rights Agreement by and among Digirad Corporation and the investors listed on the schedule attached thereto, dated April 23, 2002, as amended
31.1*	Certification of Chief Executive Officer pursuant to Rules 13a-14(a) and 15d-14(a) promulgated pursuant to the Securities Exchange Act of 1934, as amended
31.2*	Certification of Chief Financial Officer pursuant to Rules 13a-14(a) and 15d-14(a) promulgated pursuant to the Securities Exchange Act of 1934, as amended
32.1**	Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2**	Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101***	The following financial information from the Company s Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2011, formatted in XBRL (eXtensible Business Reporting Language): (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Operations, (iii) Consolidated Statements of Cash Flows, and (iv) the Notes to Consolidated Financial Statements, tagged as blocks of text.

(1) This exhibit was previously filed as an exhibit to the Company s quarterly report on Form 10-Q originally filed with the Securities and Exchange Commission on August 11, 2004, as amended thereafter, and is incorporated herein by reference.

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(2) The exhibit was previously filed as an exhibit to the Company s quarterly report on Form 8-K filed with the Securities and Exchange Commission on May 9, 2007, and is incorporated herein by reference.

(3) This exhibit was previously filed as an exhibit to the Registration Statement on Form S-1 (File No. 333-113760) originally filed with the Securities and Exchange Commission on June 19, 2004, as amended thereafter, and is incorporated herein by reference.

(4) This exhibit was previously filed as an exhibit to the Company s quarterly report on Form 10-Q filed with the Securities and Exchange Commission on November 2, 2004, and is incorporated herein by reference.

(*) Filed herewith.

(**) This certification is being furnished solely to accompany this quarterly report pursuant to 18 U.S.C. § 1350, and is not being filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and is not to be incorporated by reference into any filing of Digirad Corporation, whether made before or after the date hereof, regardless of any general incorporation language in such filing.

(***) Users of this data are advised that pursuant to Rule 406T of Regulation S-T, this XBRL information is being furnished and not filed herewith for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and Sections 11 or 12 of the Securities Act of 1933, as amended, and is not to be incorporated by reference into any filing, or part of any registration statement or prospectus, of Digirad Corporation, whether made before or after the date hereof, regardless of any general incorporation language in such filing.

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SIGNATURES

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

DIGIRAD CORPORATION

Date: July 26, 2011

By: /s/ TODD P. CLYDE
Todd P. Clyde

President and Chief Executive Officer

(Principal Executive Officer)

Date: July 26, 2011

By: /s/ RICHARD B. SLANSKY
Richard B. Slansky

Chief Financial Officer

(Principal Financial and Accounting Officer)