DYNATRONICS CORP
Form 10QSB
May 15, 2007

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

FORM 10-QSB

(Mark One)

[X] QUARTERLY REPORT UNDER SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2007.

[ ] TRANSITION REPORT UNDER SECTION 13 OR 15(D) OF THE EXCHANGE ACT

For the transition period from _________ to _________

Commission File Number: 0-12697

Dynatronics Corporation
(Exact name of small business issuer as specified in its charter)

Utah	87-0398434
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

7030 Park Centre Drive, Salt Lake City, UT 84121
(Address of principal executive offices)

(801) 568-7000
(Issuer's telephone number)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 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 is a shell company (as defined in rule 12b-2 of the Exchange Act). Yes __ No X

The number of shares outstanding of the issuer's common stock, no par value, as of May 9, 2007 is approximately 8.8 million.

Transitional Small Business Disclosure Format (Check one): Yes __ No X

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DYNATRONICS CORPORATION
Balance Sheets

Assets	March 31, 2007 (Unaudited)	June 30, 2006 (Audited)
Current assets:		
Cash	$ 467,297	423,184
Trade accounts receivable, less allowance for doubtful accounts of $271,205 at March 31, 2007 and $244,238 at June 30, 2006	3,009,736	3,022,991
Other receivables	315,828	216,847
Inventories, net	5,011,509	4,982,990
Prepaid expenses	433,590	505,786
Prepaid income taxes	262,271	65,869
Deferred tax asset - current	387,830	387,830
Total current assets	9,888,061	9,605,497

Property and equipment, net	3,473,117	3,671,216
Goodwill, net of accumulated amortization of $649,792 at March 31, 2007 and at June 30, 2006	789,422	789,422
Other assets	379,991	457,520
	$ 14,530,591	14,523,655

Liabilities and Stockholders' Equity

Current liabilities:		
Current installments of long-term debt	$ 230,331	254,518
Line of credit	1,668,018	577,232
Accounts payable	305,854	593,016
Accrued expenses	477,604	536,131
Accrued payroll and benefit expenses	147,798	254,453
Total current liabilities	2,829,605	2,215,350
Long-term debt, excluding current installments	1,854,316	2,023,410
Deferred compensation	412,415	388,250
Deferred tax liability - noncurrent	225,603	225,603
Total liabilities	5,321,939	4,852,613
Commitments		
Stockholders' equity:		
Common stock, no par value. Authorized 50,000,000 shares; issued 8,856,102 shares at March 31, 2007 and 9,034,566 shares at June 30, 2006	2,586,097	2,746,503
Deferred stock compensation	(6,000)	(4,000)
Retained earnings	6,628,555	6,928,539
Total stockholders' equity	9,208,652	9,671,042
	$ 14,530,591	14,523,655

See accompanying notes to condensed financial statements.

DYNATRONICS CORPORATION
Condensed Statements Of Operations
(Unaudited)

	Three Months Ended March 31		Nine Mo[nths Ended] Mar[ch 31]
	2007	2006	2007

Net sales	$ 4,330,440	$ 4,979,697	$ 12,897,679
Cost of sales	2,719,548	3,175,172	8,163,440
Gross profit	1,610,892	1,804,525	4,734,239
Selling, general, and administrative expenses	1,368,680	1,312,920	3,938,693
Research and development expenses	328,980	430,363	1,153,736
Operating income (loss)	(86,768)	61,242	(358,190
Other income (expense):			
Interest income	7,381	2,982	18,726
Interest expense	(54,870)	(38,856)	(155,640
Other income, net	1,919	2,580	7,326
Net other income (expense)	(45,570)	(33,294)	(129,588
Income (loss) before income taxes	(132,338)	27,948	(487,778
Income tax expense (benefit)	(50,949)	10,929	(187,794
Net income (loss)	$ (81,389)	$ 17,019	$ (299,984
Basic and diluted net income (loss) per common share	$ (0.01)	$ 0.00	$ (0.03
Weighted average basic and diluted common shares outstanding (note 2)			
Basic	8,881,534	9,022,214	8,936,425
Diluted	8,881,534	9,163,714	8,936,425

See accompanying notes to condensed financial statements.

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DYNATRONICS CORPORATION
Statements of Cash Flows
(Unaudited)

	Nine Months Ended March 31 2007	2006
Cash flows from operating activities:		
Net income (loss)	$ (299,984)	$ 154,931
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Depreciation and amortization of property and equipment	266,108	247,015

Other amortization	5,493	5,493
Provision for doubtful accounts	24,000	36,000
Provision for inventory obsolescence	126,000	189,000
Provision for warranty reserve	198,792	205,305
Provision for deferred compensation	24,165	20,799
Compensation expense on stock and options	6,374	2,000
Change in operating assets and liabilities:		
Receivables	(109,726)	(686,682)
Inventories	(154,519)	(592,808)
Prepaid expenses and other assets	144,232	(69,724)
Accounts payable and accrued expenses	(651,136)	(488,788)
Prepaid income tax	(196,402)	21,701
Income tax payable	-	17,561
Net cash used in operating activities	(616,603)	(938,197)
Cash flows from investing activities:		
Capital expenditures	(68,009)	(803,331)
Proceeds from sale of assets	-	1,500
Net cash used in investing activities	(68,009)	(801,831)
Cash flows from financing activities:		
Proceeds from issuance of long-term debt	-	1,530,000
Principal payments on long-term debt	(193,281)	(741,056)
Net change in line of credit	1,090,786	1,007,221
Proceeds from issuance of common stock	23,664	14,215
Redemption of common stock	(192,444)	-
Net cash provided by financing activities	728,725	1,810,380
Net change in cash	44,113	70,352
Cash at beginning of period	423,184	472,899
Cash at end of period	$ 467,297	$ 543,251
Supplemental disclosures of cash flow information:		
Cash paid for interest	$ 152,215	$ 101,368
Cash paid for income taxes	$ 8,608	$ 57,000
Supplemental disclosure of non-cash investing and financing activities:		
Common stock issued for directors fees	$ 8,000	$ 8,000

See accompanying notes to condensed financial statements.

DYNATRONICS CORPORATION
NOTES TO CONDENSED FINANCIAL STATEMENTS
March 31, 2007
(Unaudited)

NOTE 1. PRESENTATION

The balance sheet as of March 31, 2007 and statements of operations and cash flows for the three and nine months ended March 31, 2007 and 2006 were prepared by Dynatronics Corporation without audit pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"). Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations. In the opinion of management, all necessary adjustments, which consist only of normal recurring adjustments, to the financial statements have been made to present fairly the financial position and results of operations and cash flows. The results of operations for the respective periods presented are not necessarily indicative of the results for the respective complete years. The Company has previously filed with the SEC an annual report on Form 10-KSB which included audited financial statements for the two years ended June 30, 2006 and 2005. It is suggested that the financial statements contained in this filing be read in conjunction with the statements and notes thereto contained in the Company's 10-KSB filing.

NOTE 2. NET INCOME PER COMMON SHARE

Net income (loss) per common share is computed based on the weighted-average number of common shares and, as appropriate, dilutive common stock equivalents outstanding during the period. Stock options are considered to be common stock equivalents. The computation of diluted earnings per share does not assume exercise or conversion of securities that would have an anti-dilutive effect.

Basic net income (loss) per common share is the amount of net income (loss) for the period available to each share of common stock outstanding during the reporting period. Diluted net income (loss) per common share is the amount of net income (loss) for the period available to each share of common stock outstanding during the reporting period and to each common stock equivalent outstanding during the period, unless inclusion of common stock equivalents would have an anti-dilutive effect.

In calculating net income (loss) per common share, the net income (loss) was the same for both the basic and diluted calculation for the three and nine months ended March 31, 2007 and 2006. A reconciliation between the basic and diluted weighted-average number of common shares for the three and nine months ended March 31, 2007 and 2006 is summarized as follows:

	(Unaudited) Three Months Ended March 31,		(Unaudited) Nine Months Ended March 31,	
	2007	2006	2007	2006
Basic weighted average number of common shares outstanding during the period	8,881,534	9,022,214	8,936,425	9,020,111

Weighted average number of dilutive common stock options outstanding during the period	-	141,500	-	162,120
Diluted weighted average number of common and common equivalent shares outstanding during the period	8,881,534	9,163,714	8,936,425	9,182,231

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Outstanding options not included in the computation of diluted net income (loss) per share for the three month periods ended March 31, 2007 and 2006 total 830,757 and 648,352 respectively, and for the nine month periods ended March 31, 2007 and 2006 total 810,193 and 640,552 respectively, because to do so would have been anti-dilutive.

NOTE 3. EMPLOYEE STOCK COMPENSATION

Effective July 1, 2006, the Company adopted SFAS No. 123(R) (Revised 2004), Share Based Payment ("SFAS 123R"). SFAS 123R requires that compensation cost related to share-based payment transactions be recognized in the financial statements using a fair value method of accounting. Share-based payment transactions within the scope of SFAS 123R include stock options, restricted stock plans, performance-based awards, stock appreciation rights, and employee share purchase plans.

Using the modified prospective method, compensation cost recognized in the three and nine months ended March 31, 2007, includes amounts of compensation cost of all stock based payments that vested during the period (based on grant date fair value estimated in accordance with the original provisions of SFAS No. 123, and previously presented in the proforma footnote disclosures). In accordance with the modified prospective method, results for prior periods have not been restated.

The following table summarizes the effect during the three and nine months ended March 31, 2007 of adopting SFAS No. 123(R) as of July 1, 2006:

	Three Months March 31, 2007	Nine Months March 31, 2007
Selling, general, and administrative expenses	$ 374	741
Total stock option compensation expense recognized	374	741
Related deferred income tax expense	-	-
Increase in net loss	374 $	741
Impact on basic and diluted net income (loss) per common share	$ -	-

Prior to July 1, 2006, as permitted under SFAS No. 123, the Company accounted for its stock option plans following the recognition and measurement principles of Accounting Principles Board (APB) Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations. Accordingly, no stock based compensation had been reflected in net income (loss) for stock options granted to directors, officers and employees of the Company as all options granted had an exercise price equal to the market value of the underlying common stock on the date of grant and the related number of shares granted was fixed at that time. Had compensation expense for the Company's stock option plan been determined based on the fair value at the grant date for awards consistent with the provisions of SFAS No. 123, the Company's results of operations would have been reduced to the pro forma amounts indicated below for the periods ended March 31, 2006:

	Three Months Ended March 31, 2006	Nine Months Ended March 31, 2006
Net income (loss) as reported	$ 17,019	154,931
Less: pro forma adjustment for stock based compensation, net of income tax	(10,065)	(461,539)
Pro forma net income (loss)	$ 6,954	(306,608)
Basic and diluted net income (loss) per share:		
As reported	$ 0.00	0.02
Effect of pro forma adjustment	0.00	(0.05)
Pro forma	0.00	(0.03)

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The per share weighted-average fair value of stock options granted for the three months ended March 31, 2007 and 2006 was $0.72 and $1.16 per share, respectively, and for the nine months ended March 31, 2007 and 2006 was $0.75 and $1.23 per share, respectively, on the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions:

	Three Months Ended March 31, 2007	Three Months Ended March 31, 2006
Expected dividend yield	0%	0%
Risk-free interest rate	4.53 - 4.81%	4.34 - 4.79%
Expected volatility	55%	80 - 81%
Vesting period	4 - 5 years	1 - 5 years
Expected life	7 years	7 & 10 years

	Nine Months Ended March 31, 2007	Nine Months Ended March 31, 2006

Expected dividend yield	0%	0%
Risk-free interest rate	4.50 - 5.03%	4.14 - 4.79%
Expected volatility	55 - 58%	80 - 88%
Vesting period	4 - 5 years	0 - 5 years
Expected life	7 years	7 & 10 years

NOTE 4. COMPREHENSIVE INCOME

For the periods ended March 31, 2007 and 2006, comprehensive income was equal to the net income as presented in the accompanying condensed statements of income.

NOTE 5. INVENTORIES

Inventories consisted of the following:

	March 31, 2007	June 30, 2006
Raw material	$ 3,058,583	3,034,919
Finished goods	2,469,643	2,331,563
Inventory reserve	(516,717)	(383,492)
	$ 5,011,509	4,982,990

NOTE 6. PROPERTY AND EQUIPMENT

Property and equipment were as follows:

	March 31, 2007	June 30, 2006
Land	$ 354,744	354,743
Buildings	3,603,380	3,590,088
Machinery and equipment	1,517,465	1,481,796
Office equipment	1,078,711	1,059,664
Vehicles	94,290	94,290
	6,648,590	6,580,581
Less accumulated depreciation and amortization	3,175,473	2,909,365
	$ 3,473,117	3,671,216

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NOTE 7. PRODUCT WARRANTY RESERVE

The Company accrues the estimated costs to be incurred in connection with its product warranty programs as products are sold based on historical warranty rates. The product warranty reserve is included in accrued expenses at March 31, 2007 and 2006. A reconciliation of the changes in the warranty liability is as follows:

	Three Months Ended March 31, 2007	Three Months Ended March 31, 2006
Beginning product warranty reserve balance	$ 208,000	208,000
Warranty repairs	(64,235)	(75,462)
Warranties issued	62,157	35,466
Changes in estimated warranty costs	2,078	39,996
Ending product warranty liability balance	$ 208,000	208,000

	Nine Months Ended March 31, 2007	Nine Months Ended March 31, 2006
Beginning product warranty reserve balance	$ 208,000	208,000
Warranty repairs	(198,792)	(205,305)
Warranties issued	185,128	103,762
Changes in estimated warranty costs	13,664	101,543
Ending product warranty liability balance	$ 208,000	208,000

NOTE 8. COMMON STOCK

The Company received proceeds of $1,697 during the nine months ended March 31, 2007 for 1,664 shares of common stock that were issued upon the exercise of options by employees and $21,600 for 20,000 shares of common stock that were issued upon the exercise of options by non-employees. The Company received proceeds of $14,215 during the nine months ended March 31, 2006 for 12,886 shares of common stock that were issued upon he exercise of options by employees.

On July 15, 2003, the Company approved an open-market share repurchase program for up to $500,000 of the Company's common stock. During the nine months ended March 31, 2007, the Company acquired and retired 63,210 shares of common stock at a cost of $73,417.

NOTE 9. RECENT ACCOUNTING PRONOUNCEMENTS

In June 2006, the FASB ratified Emerging Issues Task Force Issue, or EITF, No. 06-3, How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That Is, Gross versus Net Presentation). EITF No. 06-3 requires that, for interim and annual reporting periods beginning after December 15, 2006, we disclose our policy related to the presentation of sales taxes and similar assessments related to our revenue transactions. Early adoption is permitted. Dynatronics Corporation presents revenue net of sales taxes and any similar assessments. EITF No. 06-3 had no effect on our financial position and results of operations.

On July 13, 2006, FASB Interpretation (FIN) No. 48, Accounting for Uncertainty in Income Taxes - An Interpretation of FASB No. 109, was issued. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in a company's financial statements in accordance with FASB Statement No. 109, Accounting for Income Taxes. The provisions of FIN 48 are effective for fiscal years beginning after December 15, 2006. Accordingly, the Company will implement the revised standard in the first quarter of fiscal year 2008.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements. SFAS 157 defines fair value, establishes a framework for measuring fair value, and expands disclosure requirements regarding fair value measurement. Where applicable, this statement simplifies and codifies fair value related guidance previously issued within United States of America generally accepted accounting principles. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is currently reviewing SFAS 157 and has not yet determined the impact that the adoption of SFAS 157 will have on its results of operations or financial condition.

In February 2007, the Financial Accounting Standards Board (FASB) issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities - Including an Amendment of FASB Statement No. 115". This statement permits entities to choose to measure many financial instruments and certain other items at fair value. Most of the provisions of SFAS No. 159 apply only to entities that elect the fair value option. However, the amendment to SFAS No. 115 "Accounting for Certain Investments in Debt and Equity Securities" applies to all entities with available-for-sale and trading securities. SFAS No. 159 is effective as of the beginning of an entity's first fiscal year that begins after November 15, 2007. Early adoption is permitted as of the beginning of a fiscal year that begins on or before November 15, 2007, provided the entity also elects to apply the provision of SFAS No. 157, "Fair Value Measurements". The adoption of this statement is not expected to have a material effect on the Company's financial statements.

Item 2. Management's Discussion and Analysis or Plan of Operation

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the Financial Statements (unaudited) and Notes thereto appearing elsewhere in this report on Form 10-QSB.

Results of Operations

The Company's fiscal year ends on June 30th. This report covers the third quarter ended March 31, 2007, for the Company's fiscal year ending June 30, 2007.

Net Sales

During the quarter ended March 31, 2007, the Company generated sales of $4,330,440, compared to $4,979,697 in the quarter ended March 31, 2006. For the nine months ended March 31, 2007, the Company generated sales of $12,897,679, compared to $14,568,959 in the prior year period. Lower sales of the Company's products reflects a general softening in demand for capital equipment and supplies broadly reported by our dealer network together with the impact of increased competition. To combat these trends, management is aggressively pursuing plans to position the Company to compete more effectively within the physical medicine marketplace. In addition, the Company plans to introduce an important new product in June 2007 which will be one of our highest gross margin percentage products. Management believes that practitioners will find this new product attractive from a reimbursement perspective while, at the same time, providing strong therapeutic benefit for their patients.

Gross Profit

During the quarter ended March 31, 2007, total gross profit was $1,610,892, or 37.2% of net sales, compared to $1,804,525, or 36.2% of net sales, in the quarter ended March 31, 2006. For the nine months ended March 31, 2007, total gross profit was $4,734,239, or 36.7% of net sales, compared to $5,451,272, or 37.4% of net sales, in the prior year period. Lower sales generated during the quarter and nine months ended March 31, 2007 accounted for the diminishment in gross margin compared to the prior year periods. However, for the quarter ended March 31, 2007, gross profit as a percent of sales improved one percentage point to 37.2% due to a shift in product mix toward sales of higher margin products, including the Company's aesthetic products.

Selling, general and administrative expenses

Selling, general and administrative ("SG&A") expenses for the quarter ended March 31, 2007 were $1,368,680, or 31.6% of net sales, compared to $1,312,920, or 26.4% of net sales in the prior year period. SG&A expenses for the nine months ended March 31, 2007 were $3,938,693, or 30.5% of net sales, compared to $3,884,398, or 26.7% of net sales in the prior year period. Overall SG&A expenses for the quarter and nine months ended March 31, 2007 were within 4% of the prior year's amounts. The increase in SG&A expenses is attributable to increased selling expenses associated with efforts to boost sales, increased labor expenses, and higher health insurance premiums in the quarter and nine-month periods ended March 31, 2007 compared to the prior year periods. These increased expenses were partly offset by lower general expenses.

Research and Development

R&D expenses during the quarter ended March 31, 2007 decreased to $328,980, compared to $430,363 in the prior year period. R&D expenses represented approximately 7.6% and 8.6% of the net sales of the Company in the quarters ended March 31, 2007 and 2006, respectively. For the nine months ended March 31, 2007, R&D expenses decreased to $1,153,736, compared to $1,276,329 in the prior year period. R&D costs are expensed as incurred. Development of the new X-Series products resulted in higher R&D expenses through December 2006. With that development effort now completed, R&D expenses for the third quarter decreased to levels experienced in prior years. Nevertheless, the Company remains committed to a strong R&D program in order to develop state-of-the-art products for future growth.

Other income

The Company recorded a $57,000 gain from the sale of an investment last fiscal year during the quarter ended September 30, 2005.

Pre-tax Profit/ Loss

Pre-tax loss for the quarter ended March 31, 2007 was $132,338 compared to a pre-tax profit of $27,948 in the quarter ended March 31, 2006. Pre-tax loss for the nine months ended March 31, 2007 was $487,778 compared to a pre-tax profit of $252,193 in the prior year period. As previously explained, lower sales and margins generated during the current periods resulted in the pre-tax loss in the quarter and nine months ended March 31, 2007 compared to the prior year periods.

Income Tax Benefit/Expense

Income tax benefit for the quarter ended March 31, 2007 was $50,949 compared to income tax expense of $10,929 in the quarter ended March 31, 2006. For the nine months ended March 31, 2007, income tax benefit equaled $187,794 compared to income tax expense of $97,262 in the prior year period. The effective tax rate for the quarter ended March 31, 2007 was 38.5% compared to 39.1% for the prior year period. The effective tax rate for the nine months ended March 31, 2007 was 38.5% compared to 38.6% for the prior year period.

Net Income/Loss

Net loss for the quarter ended March 31, 2007 was $81,389 ($.01 per share), compared to net income of $17,019 ($.00 per share) in the quarter ended March 31, 2006. Net loss for the nine months ended March 31, 2007 was $299,984 ($.03 per share), compared to net income of $154,931 ($.02 per share) in the similar period of the previous year. These decreases in fiscal year 2007 are primarily the result of lower sales and margins compared to the prior year periods.

Liquidity and Capital Resources

The Company has financed its operations through cash reserves, available borrowings under its line of credit, and from cash provided by operations. The Company had working capital of $7,058,456 at March 31, 2007, inclusive of the current portion of long-term obligations and credit facilities, as compared to working capital of $7,390,147 at June 30, 2006. The Company believes that it has sufficient liquidity and working capital to meet its operational requirements.

Accounts Receivable

Trade accounts receivable, net of allowance for doubtful accounts, decreased $13,255 to $3,009,736 at March 31, 2007 compared to $3,022,991 at June 30, 2006. The Company's trade accounts receivable fluctuate each quarter based on the level of sales generated during the reporting period, and the timing of payments received from its dealers, medical practitioners and clinics who are its primary customers. We estimate that the allowance for doubtful accounts is adequate based on our historical knowledge and relationships with these customers. Accounts receivable are generally collected within 30 days of the agreed terms.

Inventories

Inventories, net of reserves, at March 31, 2007 increased $28,519 to $5,011,509 compared to $4,982,990 at June 30, 2006. Inventory levels fluctuate based on the timing of the receipt of imported goods from overseas suppliers and the Company's introduction of new products. Management anticipates that inventory levels may rise by a small amount with the planned introduction of a new therapy device and treatment table in the fourth quarter of fiscal year 2007.

Prepaid Expenses

Prepaid expenses decreased $72,196 to $433,590 at March 31, 2007 compared to $505,786 at June 30, 2006, due primarily to decreases in prepaid insurance and advances made to suppliers for various component parts.

Goodwill

Goodwill at March 31, 2007 and June 30, 2006 was $789,422. Beginning July 1, 2002, the Company adopted the provisions of SFAS No. 142 Goodwill and other Intangible Assets. In compliance with SFAS 142, management utilized standard principles of financial analysis and valuation, including transaction value, market value and income value methods, to arrive at a reasonable estimate of the fair value of the Company in comparison to its book value. The Company has determined it has one reporting unit. As of July 1, 2002 and June 30, 2006, the fair value of the Company exceeded the book value of the Company. Therefore, there was no indication of impairment upon adoption of SFAS No. 142 or at June 30, 2006. Management is primarily responsible for the FAS 142 valuation determination.

Accounts Payable

Accounts payable decreased by $287,162 to $305,854 at March 31, 2007 compared to $593,016 at June 30, 2006. All accounts payable are within term. We continue to take advantage of available early payment discounts when offered.

Accrued Payroll & Benefit Expenses

Accrued payroll & benefit expenses decreased by $106,655 to $147,798 at March 31, 2007 compared to $254,453 at June 30, 2006. The decrease in accrued payroll & benefit expenses is related to: 1) timing differences resulting in lower accrued payroll at March 31, 2007 compared to June 30, 2006, and 2) lower accrued bonuses for employees and officers and corresponding payroll taxes.

Cash

The Company's cash position increased $44,113 to $467,297 at March 31, 2007 compared to $423,184 at June 30, 2006. The Company believes that its current cash balances, amounts available under its line of credit and cash provided by operations will be sufficient to cover its operating needs in the ordinary course of business for the next twelve months. If we experience an adverse operating environment or unusual capital expenditure requirements, additional financing may be required. However, no assurance can be given that additional financing, if required, would be available on favorable terms.

Line of Credit

The Company maintains a revolving line of credit with a commercial bank up to a maximum amount of $4,500,000. The outstanding balance on our line of credit increased $1,090,786 to $1,668,018 at March 31, 2007 compared to $577,232 at June 30, 2006. For a more complete explanation of the components causing this increase in borrowings, please refer to the Statement of Cash Flows included with this document. Interest on the line of credit is based on the bank's prime rate, which at March 31, 2007, was 8.25%. The line of credit is collateralized by accounts receivable and inventories. Borrowing limitations are based on 30% of eligible inventory and up to 80% of eligible accounts receivable. The line of credit is renewable biennially in December of each odd numbered year, and includes covenants requiring the Company to maintain certain financial ratios. As of March 31, 2007, the Company was in compliance with all loan covenants.

The current ratio was 3.5 to 1 at March 31, 2007 compared to 4.3 to 1 at June 30, 2006. Current assets represented 68% of total assets at March 31, 2007.

Debt

Long-term debt excluding current installments totaled $1,854,316 at March 31, 2007 compared to $2,023,410 at June 30, 2006. Long-term debt is comprised primarily of the mortgage loans on our office and manufacturing facilities in Utah and Tennessee. The current principal balance on the mortgage loans is approximately $2.1 million, with monthly principal and interest payments of $29,320.

Stock Repurchase Program

On September 3, 2003, the Company announced a stock repurchase program. The Board of Directors authorized the expenditure of up to $500,000 to purchase the Company's common stock on the open market subject to regulatory restrictions governing such repurchases. During fiscal 2004, the Company purchased $89,000 of stock. During fiscal 2006, the Company purchased $59,000 of stock. In the first three quarters of fiscal 2007, the Company purchased $192,000 of stock, leaving over $159,000 of authorized funds for future stock repurchases. The stock repurchase program is conducted subject to safe harbor regulations under Rule 10b-18 of the Exchange Act for the repurchase by an issuer of its own shares.

Inflation and Seasonality

The Company's revenues and net income from continuing operations have not been unusually affected by inflation or price increases for raw materials and parts from vendors.

The Company's business operations are not materially affected by seasonality factors.

Critical Accounting Policies

We have identified the policies below as critical to our business operations and the understanding of our results of operations. The impact and risks related to these policies on our business operations are discussed in this Management's Discussion and Analysis where such policies affect our reported and expected financial results. For a detailed discussion of the application of these and other accounting policies, see Notes to the Audited Financial Statements contained in the Company's annual report on Form 10-KSB for the year ended June 30, 2006. In all material respects, management believes that the accounting principles that are utilized conform to accounting principles generally accepted in the United States of America.

The preparation of this quarterly report requires us to make significant estimates and judgments that affect the amounts of assets, liabilities, revenues and expenses reported in our unaudited financial statements. By their nature, these judgments are subject to an inherent degree of uncertainty. We continually evaluate these estimates, including those related to bad debts, inventories, intangible assets, warranty obligations, product liability, revenue, and income taxes. We base our estimates on historical experience and other facts and circumstances that are believed to be reasonable, and the results form the basis for making judgments about the carrying value of assets and liabilities. The actual results may differ from these estimates under different assumptions or conditions.

Inventory Reserve

The nature of our business requires that we maintain sufficient inventory on hand at all times to meet the requirements of our customers. We record finished goods inventory at the lower of standard cost, which approximates actual costs (first-in, first-out), or market. Raw materials are recorded at the lower of cost (first-in, first-out) or market. Inventory valuation reserves are maintained for the estimated impairment of the inventory. Impairment may be a result of slow moving or excess inventory, product obsolescence or changes in the valuation of the inventory. In determining the adequacy of reserves, we analyze the following, among other things:

- Current inventory quantities on hand.
- Product acceptance in the marketplace.
- Customer demand.
- Historical sales.
- Forecast sales.
- Product obsolescence.
- Technological innovations.

Any modifications to estimates of inventory valuation reserves are reflected in the cost of goods sold within the statements of income during the period in which such modifications are determined necessary by management. At March 31, 2007 and June 30, 2006, our inventory valuation reserve balance was $516,717 and $383,492, respectively, and our inventory balance was $5,011,509 and $4,982,990 net of reserves, respectively.

Revenue Recognition

Our products are sold primarily to customers who are independent distributors and equipment dealers. These distributors resell the products, typically to end users, including physical therapists, professional trainers, athletic trainers, chiropractors, medical doctors and aestheticians. Sales revenues are recorded when products are shipped FOB shipping point under an agreement with a customer, risk of loss and title have passed to the customer, and collection of any resulting receivable is reasonably assured. Amounts billed for shipping and handling of products are recorded as sales revenue. Costs for shipping and handling of products to customers are recorded as cost of sales.

Allowance for Doubtful Accounts

We must make estimates of the collectibility of accounts receivable. In doing so, we analyze historical bad debt trends, customer credit worthiness, current economic trends and changes in customer payment patterns when evaluating the adequacy of the allowance for doubtful accounts. Our accounts receivable balance was $3,009,736 and $3,022,991, net of allowance for doubtful accounts of $271,205 and $244,238, at March 31, 2007 and June 30, 2006, respectively.

Business Plan and Outlook

During fiscal year 2007, management began implementing a four-fold strategy to improve overall operations. This strategy focused on (1) increasing marketing efforts through new sales incentive programs; (2) reducing manufacturing and R&D

labor expenses; (3) enhancing product profit margins through improved manufacturing processes; and (4) continuing development of new, state-of-the-art products for future growth. Management's goal in implementing this four-fold strategy is to enable the Company to address short-term profitability without jeopardizing long-term growth.

During fiscal 2007, the Company introduced several new sales incentive programs for dealers and their salespeople including an incentive cruise for fiscal 2007. In addition, management identified a number of improvements that can be made to lower manufacturing costs and plans to implement them to improve profit margins, not only for the new X-Series products but also for our other therapy equipment. The timing to implement some of these changes is dependent on exhausting current supplies of parts and identifying vendors who can assist with planned cost reductions. As a result, it is expected to take up to six months to fully implement some of these cost reductions while others will be implemented more timely. Labor cost reductions are being achieved through improved production efficiencies, trimming production staffing, and by reductions in R&D labor which had been ramped up the past year to accelerate development of the X-Series products. The Company continues development of new products for both the rehabilitation and aesthetic markets with new products scheduled for release in each of the next two quarters.

During fiscal 2007, we introduced the Dynatron X3, a powerful light therapy device capable of powering a light probe and two light pads simultaneously. This device incorporates touch screen technology for easy interface with the practitioner. We also introduced the DX2 combination traction and light therapy device. The DX2 is Dynatronics' first proprietary traction device and incorporates not only touch screen technology, but other unique and proprietary technology that will facilitate traction and decompression therapy. We believe it is the only unit on the market that offers traction and infrared light therapy from the same device. Market reception of the X3 did not meet expectations of management mostly due to the selling price of the unit. Efforts are being made to reduce costs of this unit to make it more affordable. The DX2 has performed closer to expectations and seems to have been well received as an innovative device for delivering traction and decompression therapy.

The introduction of the new T4 motorized treatment table in March 2007 and the introduction of the new T3 treatment table scheduled for the fourth fiscal quarter ending June 30, 2007, will round out the full traction package concept originally conceived. These tables are designed with a higher lift capacity and several unique features. The T4 therapy table is specially designed for performing traction and decompression therapies with the DX2 unit and has been very well received in the market.

A new therapy product is scheduled for introduction in June 2007. This new product will not replace any existing products, but serves to broaden the product line of available therapeutic modalities. Management anticipates that this new unit will carry margins well above the Company's average gross margin percentage, thus improving overall margins going forward.

Over the past two years, international sales have been maintained above the $1 million level, or approximately 5% of net sales. We continue to press forward seeking additional opportunities for international expansion. The Company's Salt Lake City operation, where all electrotherapy, ultrasound, STS devices, light therapy and Synergie products are manufactured, is certified to ISO 13485, an internationally recognized standard of excellence in medical device manufacturing. This designation is an important requirement in obtaining the CE Mark certification, which allows us to market our products in the European Union and other foreign countries. Past efforts to improve international marketing have yielded only marginal improvements. We remain committed, however, to finding the most cost effective ways to expand our markets internationally.

Marketing efforts are being increased to promote our aesthetic products which include the Synergie AMS device for dermal massage, the Synergie MDA device for microdermabrasion, and the Synergie LT device, an infrared light therapy unit designed specifically for aesthetic applications. In addition, we are redesigning our Synergie product line to give it a fresh appearance and greater functionality. We also plan to develop and introduce additional products for the aesthetic market. A new national sales manager was hired in the quarter ended December 31, 2006 with experience in setting up dealer and distributor networks. Also, Kelvyn Cullimore Sr., who managed the Synergie branded products until departing two years ago on a humanitarian mission to Asia, has returned to again manage the department. Under his prior management, Synergie branded products achieved their highest level of sustained sales. Numerous strategic partnerships are currently under consideration that would help return sales to higher levels experienced in the past.

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The dynamics of the physical medicine market are changing. Once a much fragmented market, there has been movement toward consolidation resulting in a more competitive market. Management is aggressively pursuing plans to position the company to compete more effectively within this changing marketplace. These plans include changes to our traditional models of distribution and renewed focus on establishing strategic business partnerships. Management believes these additional strategic initiatives will be responsive to the changing dynamics of the physical medicine market and, along with the aforementioned strategic initiatives, will enable the Company to improve future profitability.

Based on our defined strategic initiatives, we are focusing our resources in the following areas:

- Reinforcing our position in the physical medicine market through an aggressive marketing and advertising plan which includes several new sales incentive programs.

- Reducing manufacturing labor and certain other expenses through improved production efficiencies, reduction in personnel count and decreasing R&D labor costs which had been increased over the past year to accelerate the introduction of the X-Series products.

- Enhancing product profit margins through improved manufacturing processes, particularly for the recently introduced X-Series products.

- Continuing development of new, state-of-the-art products, both high tech and commodity, in fiscal year 2007, for both the rehabilitation and aesthetic markets.

- Improving distribution of aesthetic products domestically and exploring the opportunities to introduce more products into the aesthetics market.

- Expanding distribution of both rehabilitation and aesthetic products internationally.

- Modifying traditional distribution models to better position the Company to be responsive to the changing dynamics in the physical medicine market.

- Establishing strategic business alliances that will leverage and complement the Company's competitive strengths.

Cautionary Statement Concerning Forward-Looking Statements

The statements contained in this report on Form 10-QSB, particularly the foregoing discussion in Part 1 Item 2, Management's Discussion and Analysis or Plan of Operation, that are not purely historical, are "forward-looking statements" within the meaning of Section 21E of the Securities Exchange Act. These statements refer to our expectations, hopes, beliefs, anticipations, commitments, intentions and strategies regarding the future. They may be identified by the use of the words or phrases "believes," "expects," "anticipates," "should," "plans," "estimates," "intends," and "potential," among others. Forward-looking statements include, but are not limited to, statements contained in Management's Discussion and Analysis or Plan of Operation regarding product development, market acceptance, financial performance, revenue and expense levels in the future and the sufficiency of its existing assets to fund future operations and capital spending needs. Actual results could differ materially from the anticipated results or other expectations expressed in such forward-looking statements for the reasons detailed in our Annual Report on Form 10-KSB under the headings "Description of Business" and "Risk Factors." The fact that some of the risk factors may be the same or similar to past reports filed with the SEC means only that the risks are present in multiple periods. We believe that many of the risks detailed here and in our other SEC filings are part of doing business in the industry in which we operate and compete and will likely be present in all periods reported. The fact that certain risks are endemic to the industry does not lessen their significance.

The forward-looking statements contained in this report are made as of the date of this report and we assume no obligation to update them or to update the reasons why actual results could differ from those projected in such forward-looking statements. Among others, risks and uncertainties that may affect the business, financial condition, performance, development, and results of operations include:

- market acceptance of our technologies, particularly our core therapy devices, Synergie AMS/MDA product line, and the Solaris infrared light therapy products;

- failure to timely release new products against market expectations;

- the ability to hire and retain the services of trained personnel at cost-effective rates;

- rigorous government scrutiny or the possibility of additional government regulation of the industry in which we market our products;

- reliance on key management personnel;

- foreign government regulation of our products and manufacturing practices that may bar or significantly increase the expense of expanding to foreign markets;

- economic and political risks related to expansion into international markets;

- failure to sustain or manage growth, including the failure to continue to develop new products or to meet demand for existing products;

- reliance on information technology;
- the timing and extent of research and development expenses;
- the ability to keep pace with technological advances, which can occur rapidly;
- the loss of product market share to competitors;
- potential adverse effect of taxation;
- additional terrorist attacks on U.S. interests and businesses;
- the ability to obtain required financing to meet changes or other risks; and
- escalating costs of raw materials, particularly steel and petroleum based materials.

As a public company, we are subject to the reporting requirements of the Securities Exchange Act of 1934 and the Sarbanes-Oxley Act of 2002. These requirements may place a strain on our systems and resources. The Securities Exchange Act requires, among other things, that we file annual, quarterly and current reports with respect to our business and financial condition. The Sarbanes-Oxley Act requires, among other things, that we maintain effective disclosure controls and procedures and internal controls over financial reporting. We are currently reviewing and further documenting our internal control procedures. However, the guidelines for the evaluation and attestation of internal control systems for small companies continue to evolve. Therefore, we can give no assurances that our systems will satisfy the new regulatory requirements. In addition, in order to maintain and improve the effectiveness of our disclosure controls and procedures and internal controls over financial reporting, significant resources and management oversight will be required.

Item 3. Controls and Procedures

Based on evaluation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Exchange Act), as of the end of the period covered by this Report, our principal executive and principal financial officers have concluded that our disclosure controls and procedures are effective at the reasonable assurance level. There were no changes in our internal control over financial reporting that occurred during the quarter ended March 31, 2007 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

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

Small Business Issuer Purchases of Equity Securities*

		Total # of Shares Purchased as part of	Approximate Dollar Value of Shares that May
	Average		

Period	Total # of Shares Purchased	Price Paid per Share	Publicly Announced Plans or Programs	Yet be Purchased Under Plan/ Program
1/1/07 to 1/31/07	18,158	$1.19	18,158	$210,940
2/1/07 to 2/28/07	28,574	$1.18	28,574	$177,330
3/1/07 to 3/31/07	16,478	$1.11	16,478	$159,107

* The Company's repurchase program was announced on September 3, 2003. At that time, the Company approved repurchases aggregating $500,000.

Item 6. Exhibits

(a) Exhibits

3.1 Articles of Incorporation and Bylaws of Dynatronics Laser Corporation. Incorporated by reference to a Registration Statement on Form S-1 (No. 2-85045) filed with the SEC and effective November 2, 1984

3.2 Articles of Amendment dated November 21, 1988 (previously filed)

3.3 Articles of Amendment dated November 18, 1993 (previously filed)

10.1 Employment contract with Kelvyn H. Cullimore, Jr. (previously filed)

10.2 Employment contract with Larry K. Beardall (previously filed)

10.3 Loan Agreement with Zions Bank (previously filed)

10.5 Amended Loan Agreement with Zions Bank (previously filed)

10.6 1992 Amended and Restated Stock Option Plan (previously filed)

10.7 Dynatronics Corporation 2006 Equity Incentive Award Plan (previously filed as Annex A to the Company's Definitive Proxy Statement on Schedule 14A filed on October 27, 2006)

10.8 Form of Option Agreement for the 2006 Equity Incentive Plan for incentive stock options (previously filed as Exhibit 10.8 to the Company's Annual Report on Form 10-KSB for the fiscal year ended June 30, 2006)

10.9 Form of Option Agreement for the 2006 Equity Incentive Plan for non-qualified options (previously filed as Exhibit 10.9 to the Company's Annual Report

	on Form 10-KSB for the fiscal year ended June 30, 2006)
11	Computation of Net Income per Share (included in Notes to Consolidated Financial Statements)

31.1	Certification under Rule 13a-14(a)/15d-14(a) of principal executive officer (filed herewith)
31.2	Certification under Rule 13a-14(a)/15d-14(a) of principal financial officer (filed herewith)
32	Certifications under Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. SECTION 1350) (filed herewith)

SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

DYNATRONICS CORPORATION
Registrant

Date 5/14/07

/s/ Kelvyn H. Cullimore, Jr.

Kelvyn H. Cullimore, Jr.
Chairman, President and Chief Executive Officer
(Principal Executive Officer)

Date 5/14/07

/s/ Terry M. Atkinson, CPA

Terry M. Atkinson, CPA
Chief Financial Officer
(Principal Financial Officer)
