DYNATRONICS CORP
Form 10QSB
November 19, 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 September 30, 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 November 12, 2007 is approximately 13.7 million.

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

DYNATRONICS CORPORATION

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DYNATRONICS CORPORATION
Condensed Consolidated Balance Sheets
(Unaudited)

Assets

	September 30, 2007	June 30, 2007
Current assets:		
Cash	$ 289,016	1,301,105
Trade accounts receivable, less allowance for doubtful accounts of $303,272 at September 30, 2007 and $330,857 at June 30, 2007	6,041,592	3,757,484
Other receivables	312,849	282,741

Inventories, net	6,663,020	5,313,984
Prepaid expenses	570,276	507,755
Prepaid income taxes	93,249	92,702
Deferred tax asset - current	415,808	396,156
Total current assets	14,385,810	11,651,927
Property and equipment, net	3,632,465	3,453,495
Goodwill, net	6,340,211	2,758,572
Intangible asset, net	698,164	356,792
Other assets	353,040	346,830
	25,409,690	18,567,616

Liabilities and Stockholders' Equity

Current liabilities:		
Current installments of long-term debt	315,725	271,979
Line of credit	3,803,984	250,000
Warranty reserve	208,000	208,000
Accounts payable	1,808,830	1,241,030
Accrued expenses	557,886	287,773
Accrued payroll and benefit expenses	339,116	276,754
Acquisition cash obligations	618,500	1,000,000
Total current liabilities	7,652,041	3,535,536
Long-term debt, excluding current installments	3,241,529	3,251,631
Deferred compensation	428,525	420,470
Deferred tax liability - noncurrent	82,385	289,335
Total liabilities	11,404,480	7,496,972
Commitments and contingencies		
Stockholders' equity:		
Common stock, no par value. Authorized 50,000,000 shares; issued 13,672,495 shares at September 30, 2007 and 10,308,522 shares at June 30, 2007	7,873,916	4,227,147
Retained earnings	6,131,294	6,843,497
Total stockholders' equity	14,005,210	11,070,644
	$ 25,409,690	18,567,616

See accompanying notes to condensed consolidated financial statements.

DYNATRONICS CORPORATION
Condensed Consolidated Statements of Operations
(Unaudited)

Three Months Ended
September 30

	2007	2006
Net sales	$ 7,891,430	4,139,057
Cost of sales	4,959,118	2,646,900
Gross profit	2,932,312	1,492,157
Selling, general, and administrative expenses	3,575,495	1,261,145
Research and development expenses	338,893	478,084
Operating loss	(982,076)	(247,072)
Other income (expense):		
Interest income	4,915	6,683
Interest expense	(135,246)	(47,510)
Other income, net	3,164	3,332
Total other income (expense)	(127,167)	(37,495)
Loss before income taxes	(1,109,243)	(284,567)
Income tax expense (benefit)	(397,040)	(109,559)
Net loss	$ (712,203)	(175,008)
Basic and diluted net loss per common share	$ (0.05)	(0.02)
Weighted average basic and diluted common shares outstanding	13,607,666	8,976,744

See accompanying notes to condensed consolidated financial statements.

DYNATRONICS CORPORATION
Condensed Consolidated Statements of Cash Flows
(Unaudited)

	Three Months Ended September 30 2007	2006
Cash flows from operating activities:		
Net loss	$ (712,203)	(175,008)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization of property and equipment	84,927	89,750

Amortization of intangible assets	25,028	1,831
Stock based compensation expense	256,991	2,093
Provision for doubtful accounts	129,900	12,000
Provision for inventory obsolescence	42,000	48,000
Provision for warranty reserve	60,888	70,133
Provision for deferred compensation	8,055	8,055
Change in operating assets and liabilities:		
Receivables	(1,047,970)	111,851
Inventories	(138,513)	(207,835)
Prepaid expenses and other assets	(63,949)	(81,327)
Deferred tax asset, net	(401,790)	-
Accounts payable and accrued expenses	(547,121)	(118,471)
Prepaid income taxes	(547)	(109,559)
Net cash used in operating activities	(2,304,304)	(348,487)
Cash flows from investing activities:		
Capital expenditures	(60,999)	(40,419)
Business acquisitions	(1,135,692)	-
Net cash used in investing activities	(1,196,691)	(40,419)
Cash flows from financing activities:		
Principal payments on long-term debt	(56,490)	(63,405)
Net change in line of credit	2,553,984	295,533
Proceeds from issuance of common stock	29,327	21,600
Redemption of common stock	(37,915)	(41,000)
Net cash provided by financing activities	2,488,906	212,728
Net change in cash	(1,012,089)	(176,178)
Cash at beginning of period	1,301,105	423,184
Cash at end of period	$ 289,016	247,006
Supplemental disclosures of cash flow information:		
Cash paid for interest	$ 115,622	48,018
Cash paid for income taxes	1,000	-
Supplemental disclosure of non-cash investing and financing activities:		
Stock based compensation see note 3 for details		
Business acquisition disclosure see note 9 for details		
Capital expenditures financed by long term debt	90,134	-
Acquisition cash obligation financed by		

line of credit	1,000,000	-

See accompanying notes to condensed consolidated financial statements.

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DYNATRONICS CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2007
(Unaudited)

NOTE 1. PRESENTATION

The condensed consolidated balance sheet as of September 30, 2007 and condensed consolidated statements of operations and cash flows for the three months ended September 30, 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, 2007 and 2006. 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 months ended September 30, 2007 and 2006. A reconciliation between the basic and diluted weighted-average number of common shares for the three months ended September 30, 2007 and 2006 is summarized as follows:

(Unaudited)

	Three Months Ended September 30, 2007	2006
Basic weighted average number of common shares outstanding during the period	13,607,666	8,976,744
Weighted average number of dilutive common stock options outstanding during the period	-0-	-0-
Diluted weighted average number of common and common equivalent shares outstanding during the period	13,607,666	8,976,744

NOTE 3. STOCK BASED 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 months ended September 30, 2006, 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 months ended September 30, 2007 and 2006 of adopting SFAS No. 123(R) as of July 1, 2006 for the options granted:

	September 30, 2007	September 30, 2006
Selling, general, and administrative expenses	$ 494	93
Total stock option compensation expense recognized	494	93
Related deferred income tax expense	-0-	-0-
Increase in net loss	$ 494	93
Impact on basic and diluted net income (loss) per common share	$ -0-	-0-

During the quarter the Company granted 220,000 shares of stock to employees that fully vested during the quarter resulting in a non-recurring compensation expense of $238,950, an additional 80,000 shares were issued with a four year vesting which resulted in an additional $11,250 in compensation expense for the quarter.

NOTE 4. COMPREHENSIVE INCOME

For the periods ended September 30, 2007 and 2006, comprehensive income was equal to the net income as presented in the accompanying condensed consolidated statements of operations.

NOTE 5. INVENTORIES

Inventories consisted of the following:

	September 30, 2007	June 30, 2007
Raw material	$ 3,419,887	2,961,653
Finished goods	3,519,698	2,646,141
Inventory reserve	(276,565)	(293,810)
	$ 6,663,020	5,313,984

NOTE 6. PROPERTY AND EQUIPMENT

Property and equipment were as follows:

	September 30, 2007	June 30, 2007
Land	$ 354,743	354,743
Buildings	3,613,264	3,603,380
Machinery and equipment	1,622,879	1,521,601
Office equipment	1,227,216	1,147,667
Vehicles	168,310	95,124
	6,986,412	6,722,515
Less accumulated depreciation and amortization	3,353,947	3,269,020
	$ 3,632,465	3,453,495

NOTE 7. PRODUCT WARRANTY RESERVE

The Company adopted the provisions of FASB Interpretation No. 45, Guarantors' Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others, as of December 31, 2002. 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 September 30, 2007 and 2006. A reconciliation of the changes in the warranty liability is as follows:

	Three months ended September 30, 2007	Three months ended September 30, 2006
Beginning product warranty reserve balance	$ 208,000	208,000
Warranty repairs	(60,888)	(70,133)
Warranties issued	119,507	59,410
Changes in estimated warranty costs	(58,619)	10,723
Ending product warranty liability balance	$ 208,000	208,000

NOTE 8. COMMON STOCK.

The Company received proceeds of $29,326 during the three months ended September 30, 2007 for 29,889 shares of common stock that were issued upon the exercise of options for services.

NOTE 9. ACQUISITION AND NON-CASH DISCLOSURE

On July 2, 2007, the Company completed the acquisition of a 100% interest in five of its key independent distributors, Responsive Providers, Inc. of Houston, Texas, Therapy and Health Care Products, Inc. of Youngstown, Ohio, Cyman Therapy, Inc. of Detroit, Michigan, Al Rice and Associates, Inc. of Jeffersonville, Indiana and Theratech Inc. of Minneapolis, Minnesota. The total consideration paid for the five separately-negotiated acquisitions was approximately $5.6 million comprised of approximately $2.3 million in cash and 3,061,591 shares of common stock. As of September 30, 2007 there remains a cash obligation of $618,500.

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The acquisition value of the five dealers acquired was accounted for using the purchase method of accounting. Accordingly, the purchase price was assigned to the assets acquired and the liabilities assumed based on fair values at the purchase date. The following table reflects the unaudited estimated fair values of the assets acquired and the liabilities assumed as of the acquisition date:

Cash	$ 651,828
Trade accounts receivable	1,188,583
Inventories	1,252,523
Prepaid expenses	4,782
Property and equipment, net	112,764
Cash surrender value of life insurance	207,563
Intangible assets - weighted average 9 years	366,400
Goodwill	3,251,910
Total assets acquired	7,036,354
Accounts payable and accrued expenses	(1,390,199)
Net assets acquired	5,646,155

The acquisition resulted in a $145,462 deferred income tax liability and an increase to goodwill of $145,462.

Unaudited pro forma results of operations for the three months ended September 30, 2007 and 2006, as though the five dealers had been acquired as of July 1, 2006, are as follows:

	September 30, 2007	September 30, 2006
Net sales	$ 7,891,430	6,299,539
Net loss	(712,203)	(140,525)
Basic and diluted net income (loss) per common share	(.05)	.02

NOTE 10. GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill. The cost of acquired companies in excess of the fair value of the net assets and purchased intangible assets at acquisition date is recorded as goodwill. As of June 30, 2007, the Company had net goodwill of $2,758,572 arising from the acquisition of Superior Orthopaedic Supplies, Inc. on May 1, 1996, the exchange of Dynatronics Laser Corporation common stock for a minority interest in Dynatronics Marketing Corporation on June 30, 1983 and the acquisition of Rajala Therapy Sales Associates, Inc. on June 30, 2007. During the three months ended September 30, 2007 the Company recorded additional goodwill in the amount of $3,581,639 in conjunction with the acquisition of Responsive Providers, Inc., Therapy and Health Care Products, Inc., Cyman Therapy, Inc., Al Rice and Associates, Inc. and Theratech Inc.

Identifiable Intangibles. Identifiable intangibles assets, included in other assets, consists of the following:

	As of September 30, 2007	As of June 30, 2007
Trade name - 15 years	$ 339,400	118,000
Domain name - 15 years	5,400	1,200
Non-compete covenant - 4 years	149,400	114,000
Customer relationships - 7-15 years	120,000	89,000
Trademark licensing agreement - 20 years	45,000	-0-
Backlog of orders - 3 months	2,700	2,700
Customer database - 7 years	38,100	8,700
License agreement - 10 years	73,240	73,240
Total identifiable intangibles	773,240	406,840
Accumulated amortization	75,077	50,048
Net carrying amount	$ 698,164	356,792

NOTE 11. RECENT ACCOUNTING PRONOUNCEMENTS

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 adopted the revised standard during the quarter ended September 30, 2007. The adoption of this standard had no material impact on the Company's financial statements.

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 for financial assets and November 15, 2008 for non-financial assets, 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.

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 first quarter ended September 30, 2007, for the Company's fiscal year ending June 30, 2008.

Net Sales

During the quarter ended September 30, 2007, the Company's sales increased 91% to $7,891,430, compared to $4,139,057 in the quarter ended September 30, 2006. The increase in sales reflects the acquisition of six of the Company's top distributors of physical medicine products. On June 30, 2007, we acquired our largest independent distributor, Rajala Therapy Sales Associates of Pleasanton, California. On July 2, 2007, Dynatronics acquired five additional independent distributors: Responsive Providers, Inc. of Houston, Texas; Therapy and Health Care Products, Inc. of Girard, Ohio; Cyman Therapy, Inc. of Detroit, Michigan; Al Rice and Associates, Inc. of Jeffersonville, Indiana; and Theratech, Inc. of Minneapolis, Minnesota. The vertical integration of these distributors is a key strategic step toward strengthening our distribution channels. We believe that these acquisitions, as they are fully assimilated into our business operations, will provide Dynatronics with more effective direct distribution of our products and result in better margins on each product sold at the retail level compared to the wholesale level. Subsequent to these acquisitions, we have added six new direct sales persons in other territories including Southern California, Louisiana, Kansas, Oklahoma, and Wisconsin, expanding our direct sales channels to now cover 23 states.

The dealers acquired at the beginning of the quarter ended September 30, 2007, sold products from many manufacturers, including Dynatronics. As a result of the transactions described above, the mix between sales of manufactured and distributed products during the quarter covered by this report shifted toward distributed products with 42% of sales attributed to sales of distributed products and the remaining 58% being manufactured products. We anticipate the mix between manufactured and distributed products in future periods will be similar to the mix experienced during the first quarter of fiscal year 2008.

Sales of the Company's aesthetic products increased 81% during the quarter ended September 30, 2007 compared to the prior year period. The Company is experiencing a renewed emphasis in sales of its Synergie brand of aesthetic products and plans to expand and update this product line during fiscal year 2008.

Gross Profit

During the quarter ended September 30, 2007, total gross profit increased 97% to $2,932,312, or 37.2% of net sales, compared to $1,492,157, or 36.1% of net sales, in the quarter ended September 30, 2006. The increase in gross profit was primarily a result of the increased sales from the recent acquisitions. For the quarter ended September 30, 2007, gross profit as a percent of sales improved one percentage point to 37.2% due to the higher margins associated with selling at the retail level compared to the wholesale level, as well as the increase in sales of high-margin aesthetic products.

Non-recurring items affecting gross profit for the quarter ended September 30, 2007 totaled approximately $330,000 and were related to inventories of Dynatronics manufactured products acquired from the six independent dealers which had a higher cost basis because they were based on the dealer's cost of acquiring those products from us. After the higher cost basis inventory is sold over the course of the next quarter, gross profit is expected to improve.

Additionally, it should be noted that sales of distributed items typically carry lower margins than those that are manufactured. A change in the mix of product sales toward a greater percentage of distributed products reduces gross profit margins as a percent of sales.

Selling, general and administrative expenses

Selling, general and administrative ("SG&A") expenses for the quarter ended September 30, 2007 increased $2,314,350 to $3,575,495, or 45.3% of net sales, compared to $1,261,145, or 30.5% of net sales in the prior year period. Substantially all of the increase in SG&A expenses is related to the recent acquisitions and includes the following:

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- $1,116,200 in higher selling expenses related to commissions to the new direct sales force
- $621,500 in higher general and administrative expenses associated with the acquired companies
- $569,800 in higher labor and operating costs to support the higher sales volume
- $7,000 of other miscellaneous items

Non-recurring expense items along with other costs related primarily to the assimilation of the Company's six acquisitions totaled approximately $750,000 during the quarter ended September 30, 2007 and are itemized as follows:

- Stock Grant expenses $250,000
- Reserve adjustments for bad debt $118,000
- Personnel related costs* $306,000
- Other assimilation expenses $ 76,000

* Personnel related costs related to the assimilation of the Company's six acquisitions include overtime costs, severance costs, one-time bonuses, and other personnel costs.

Research and Development

R&D expenses during the quarter ended September 30, 2007 decreased to $338,893, compared to $478,084 in the prior year period. R&D expenses represented approximately 4.3% and 11.6% of the net sales of the Company in the quarters ended September 30, 2007 and 2006, respectively. R&D expenditures as a percentage of sales were lower due to the 91% increase in sales during the quarter. R&D costs are expensed as incurred. Development of the new X-Series products resulted in higher R&D expenses in the 2006 period. With the development effort for the new X-Series products now completed, R&D expenses for the first quarter decreased to standard levels experienced in prior years. Dynatronics intends to continue its commitment to developing innovative products for the physical medicine market in fiscal year 2008 and beyond in order to position the Company for growth.

Pre-tax Loss

Pre-tax loss for the quarter ended September 30, 2007 was $1,109,243 compared to a pre-tax loss of $284,567 in the quarter ended September 30, 2006. Non-recurring items along with costs related primarily to the Company's six acquisitions totaled approximately $1.1 million during the current period and was a significant factor in the increase in pre-tax loss in the quarter ended September 30, 2007 compared to the prior year period. Absent these non-recurring and acquisition related expenses, we believe we achieved a virtual operational break-even during the quarter compared to the reported loss in the same quarter last year.

Income Tax Benefit

Income tax benefit for the quarter ended September 30, 2007 was $397,040 compared to income tax benefit of $109,559 in the quarter ended September 30, 2006. The effective tax rate for the quarter ended September 30, 2007 was 35.8% compared to 38.5% for the prior year period. The lower tax rate for this quarter reflects the assumption of certain anticipated tax benefits that will be earned during the year.

Net Loss

Net loss for the quarter ended September 30, 2007 was $712,203 ($.05 per share), compared to net loss of $175,008 ($.02 per share) in the quarter ended September 30, 2006. As previously explained, non-recurring items along with costs related primarily to the Company's six acquisitions totaled approximately $1.1 million during the current period and contributed to the increase in net loss in the quarter ended September 30, 2007 compared to the prior year period.

Liquidity and Capital Resources

The Company has financed its operations through available cash reserves and available borrowings under its line of credit. The Company had working capital of $6,733,769 at September 30, 2007, inclusive of the current portion of long-term obligations and credit facilities, as compared to working capital of $8,116,391 at June 30, 2007. The $1.4 million decrease in working capital is a direct result of an increase in the line of credit required to pay the consideration associated with the recent acquisitions. Current assets during the quarter ended September 30, 2007 increased $2.7 million while current liabilities increased $4.1 million. The assumption of the dealers' assets and liabilities increased our net assets by $2.1 million, but it also increased liabilities by $1.4 million.

Accounts Receivable

Trade accounts receivable, net of allowance for doubtful accounts, increased $2,284,108 to $6,041,592 at September 30, 2007 compared to $3,757,484 at June 30, 2007. The majority of this increase in trade accounts receivable was a result of the recent acquisitions concluded during the quarter.

Trade accounts receivable represent amounts due from the Company's dealer network, from medical practitioners and clinics. We estimate that the allowance for doubtful accounts is adequate based on our historical knowledge and relationship with these customers. Accounts receivable are generally collected within 30 days of the agreed terms. However, as a result of the recent acquisitions, the character of the accounts receivable and collection patterns are anticipated to change and will be carefully monitored over the coming year to ensure the allowances are adequate.

Inventories

Inventories, net of reserves, at September 30, 2007 increased $1,349,036 to $6,663,020 compared to $5,313,984 at June 30, 2007. This increase is primarily a result of the inventories acquired in connection with the recent acquisitions. Inventories are expected to generally remain at current levels during fiscal year 2008 as we consolidate the inventories of the companies acquired into central warehouses. However, should the Company make additional acquisitions during fiscal year 2008, inventory levels would likely increase.

Goodwill

Goodwill at September 30, 2007 increased to $6,340,211 compared to $2,758,572 at June 30, 2007, due to the acquisition of the distributors on July 2, 2007.

Beginning July 1, 2002, the Company adopted the provisions of SFAS No. 142 Goodwill and other Intangible Assets. In compliance with SFAS No. 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, 2007, 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, 2007. Management is primarily responsible for the SFAS No. 142 valuation determination and performed the annual impairment assessment during the Company's fourth quarter.

Accounts Payable

Accounts payable increased $567,800 to $1,808,830 at September 30, 2007 compared to $1,241,030 at June 30, 2007, primarily as a result of the recent acquisitions. All accounts payable are within term. We continue to take advantage of available early payment discounts when offered.

Accrued Expenses and Acquisition Cash Obligation

Accrued expenses increased $270,113 to $557,886 at September 30, 2007 compared to $287,773 at June 30, 2007. Acquisition cash obligations decreased $381,500 to $618,500 at September 30, 2007 compared to $1,000,000 at June 30, 2007. This obligation reflects certain cash amounts that were placed into escrow in conjunction with the acquisitions made on June 30, 2007 and July 2, 2007.

Accrued Payroll & Benefit Expenses

Accrued payroll & benefit expenses remained relatively constant at $339,116 at September 30, 2007 compared to $276,754 at June 30, 2007.

Cash

The Company's cash position decreased to $289,016 compared to $1,301,105 at June 30, 2007 as a result of payments related to the acquisitions made on June 30, 2007 and July 2, 2007. The Company had deposited the financing proceeds in anticipation of the acquisitions, which temporarily increased cash balances at June 30, 2007. 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

In June 2007, the Company increased its revolving line of credit with a commercial bank to $6,000,000 in anticipation of making acquisitions. At September 30, 2007, the Company owed $3,803,984 compared to $250,000 at June 30, 2007. The Company used approximately $3.3 million under the line of credit to finance the recent acquisitions. Interest on the line of credit is based on the bank's prime rate, which at September 30, 2007, equaled 8.25%. The line of credit is collateralized by accounts receivable and inventories of the Company. Borrowing limitations are based on 35% of eligible inventory and up to 80% of eligible accounts receivable. Interest payments on the line are due monthly. The line of credit is renewable biennially on December 15th and includes covenants requiring the Company to maintain certain financial ratios. As of September 30, 2007, the Company was in compliance with all loan covenants or had received waivers due to acquisition activity unrelated to operating expenses.

The current ratio was 1.9 to 1 at September 30, 2007 compared to 3.3 to 1 at June 30, 2007. Current assets represented 57% of total assets at September 30, 2007 compared to 63% at June 30, 2007.

Debt

Long-term debt excluding current installments totaled $3,241,529 at September 30, 2007 compared to $3,251,631 at June 30, 2007. In June 2007, we obtained $1.5 million of long-term mortgage financing used to finance our acquisitions in June and July 2007. The funding of this loan temporarily increased our cash balances at the end of June 2007. Long-term debt is comprised primarily of the mortgage loans on our office and manufacturing facilities in Utah and Tennessee. The principal balance on the mortgage loans is approximately $3.7 million with monthly principal and interest payments of $40,707.

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. 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 reported 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. On an on-going basis, we evaluate these estimates, including those related to bad debts, inventories, and revenue recognition. 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 Reserves

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.
- Character of the inventory whether it is a distributed item, finished manufactured item or raw material.

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 September 30, 2007 and June 30, 2007, our inventory valuation reserve balance, which established a new cost basis, was $276,565 and $293,810, respectively, and our inventory balance was $6,663,020 and $5,313,984 net of reserves, respectively.

Revenue Recognition

The majority of our product sales for the past two fiscal years were to customers who are independent distributors. Beginning in the quarter ended September 30, 2007, a portion of our sales were generated through our new direct sales force which covers 23 states. Our sales force and distributors sell our products to end users, including physical therapists, professional trainers, athletic trainers, chiropractors, medical doctors and aestheticians. With the recent acquisition of six of our independent distributors, we have reduced our dependence on distributor sales. 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 $6,041,592 and $3,757,484, net of allowance for doubtful accounts of $303,272 and $330,857, at September 30, 2007 and June 30, 2007, respectively. The expansion of our customer base associated with more direct sales will spread bad debt risk over a broader base of customers and reduce the concentration of large dealer balances. At the same time, the management of more customer accounts presents a higher risk. These risks will be evaluated over the coming year to determine if current estimate policies are still applicable.

Business Plan and Outlook

During fiscal year 2008, management will continue to implement a four-fold strategy to improve overall operations. This strategy focuses on (1) strengthening distribution channels; (2) developing new, state-of-the-art products for future growth; (3) refining operations associated with the acquired companies; and (4) enhancing product profit margins through improved manufacturing processes. Management's goal in implementing this four-fold strategy is to enable the Company to address short-term profitability without jeopardizing long-term growth.

Our primary market, the physical medicine marketplace, has experienced significant change over the past few years, most notably with consolidation among manufacturers and distributors. In order to compete more favorably and effectively, our management moved aggressively to strengthen the Company's channels of distribution by acquiring key distributors. We identified six key distributors with operations in 20 states. On June 30, 2007, Dynatronics acquired its largest independent distributor headquartered in California. On July 2, 2007, Dynatronics acquired five additional key independent distributors headquartered in Texas, Ohio, Michigan, Indiana and Minnesota. Dynatronics also began hiring direct sales representatives in key locations around the country resulting in direct sales representatives now in 23 states. The creation of a direct distribution channel through these key acquisitions and hiring direct sales representatives provides Dynatronics with expanded ability to sell at the retail level, which will improve gross profit margins and enhance the Company's control over the distribution process. We expect these changes will open new opportunities for improving future sales as we continue to pursue our strategy of strengthening our distribution channels through consideration of additional acquisitions, the expansion of our direct sales force, and maximizing our relationships with strong independent dealers.

Over the past fiscal year, we introduced some important new products including 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.

The introduction of the new T4 motorized treatment table in March 2007 and the introduction of the new T3 treatment table in July 2007 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.

In June 2007, we introduced the Dynatron X-5 Oscillation Therapy device. The unique product effectively reduces pain through the creation of an electrostatic field within the patient by combining the concepts of electrotherapy with therapeutic massage. Initial sales of this product exceeded management's projections. The X5 unit's gross profit margin as a percent of sales is one of the highest of any of the therapy devices produced by Dynatronics.

The assimilation of the six acquired distributors remains the current focus of management. Since the acquisitions were completed, two of the six local operations have been closed and fully assimilated. Three of the four remaining distributors are being reduced in scope relative to operations and should be mostly assimilated by the end of December or January. Sales and sales support staff are being maintained at the four remaining operations, but warehousing functions are being consolidated to our facilities in Tennessee and Utah as well as the new facility established in California that was associated with the acquisition of Rajala Therapy Sales Associates. The ability to timely service west coast customers was deemed a critical point of service and warranted the continuance of the Rajala operations. Other areas of the country could be adequately served from these warehouse operations. The non-recurring items along with costs related primarily to the Company's six acquisitions totaled approximately $1.1 million during the first quarter. We believe the process of full integration will be ongoing for the next year, but the elimination of most duplicative expenses and the achievement of economies of scale are anticipated to be more fully realized during the third quarter of this fiscal year. We believe the second quarter of the fiscal year will show a significant decrease in non-recurring and acquisition related items, but not a total elimination.

International sales is viewed as having untapped potential for growth and expansion. Adding new distributors in several countries will be the key to this expansion effort. 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. 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.

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. 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 leadership, sales momentum of Synergie branded products has continued to mount with sales for the quarter ended September 30, 2007 up 81% compared to the similar quarter of the prior year. Numerous strategic partnerships, both domestic and international, are currently under consideration that would help maintain the sales momentum that is being built.

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

- o Reinforcing our position in the physical medicine market by securing channels of distribution through a strategy of acquiring dealers, recruiting direct sales representatives and working closely with the most successful dealers of capital equipment.

- o Continuing development of new, state-of-the-art products, both high tech and commodity, in fiscal year 2008, for both the rehabilitation and aesthetic markets.

- o Improving efficiencies in conjunction with the assimilation of the companies acquired.

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

- o Expanding distribution of both rehabilitation and aesthetic products internationally.

- o 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 I 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:

- Assimilating acquired companies in a timely and effectively manner including specific risks of:
  - Failure to realize expected economies of scale and efficiencies of operations
  - Inability to achieve sales targets
  - Loss of key sales personnel
  - Inefficiencies in management of receivables
  - Lack of controlling inventories and consolidation of inventories
  - Operational inefficiencies resulting in unmet customer expectations

- 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;

- o reliance on information technology;

- o the timing and extent of research and development expenses;
- o the ability to keep pace with technological advances, which can occur rapidly;
- o the loss of product market share to competitors;
- o potential adverse effect of taxation;
- o additional terrorist attacks on U.S. interests and businesses;
- o the ability to obtain required financing to meet changes or other risks;
- o escalating costs of raw materials, particularly steel and petroleum based materials; and
- o increased competition from a consolidating market that could put pressure on pricing and margin realization.

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 September 30, 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

The following table summarizes purchases of the Company's common stock made by the Company during the quarter ended September 30, 2007, under a stock repurchase program approved by the board of directors of the Company in September 2003.

Small Business Issuer Purchases of Equity Securities*

Period	Total # of Shares Purchased	Average Price Paid per Share	Total # of Shares Purchased as part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet be Purchased Under Plan/Program
7/1/07 to 7/31/07	-0-	N/A	N/A	$106,869
8/1/07 to 8/31/07	9,900	$1.35	9,900	$93,516
9/1/07 to 9/30/07	17,607	$1.39	17,607	$68,954

* 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 11/19/07 /s/ Kelvyn H. Cullimore, Jr.

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

Date 11/19/07 /s/ Terry M. Atkinson, CPA

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